Central American Currency and Finance

By JOHN PARKE YOUNG

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CENTRAL AMERICAN CURRENCY AND FINANCE

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With an Introduction by
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Preface

THIS book contains an account of the currency systems and recent financial developments in Central America. It does not pretend to cover the entire realm of finance, including such things as taxation and other phases of public finance, but deals especially with currency matters, foreign trade, exchange rates, and the financial relations between the United States and these countries.

The material for the book was gathered during several months' stay in Central America, during which time the capitals and important towns of all the countries were visited, and also from various sources in the United States. Obstacles in the way of obtaining reliable information were many. Records kept are meager and the material is often not in systematic or readily available form. Official publications can not be relied upon and statistics are frequently given with insufficient explanation at to what they represent. Much of the information was secured through personal interviews, but different versions of an event or situation are often very inconsistent.

Customs and financial practices in Central America differ so greatly from those of the United States that it is difficult for Americans to appreciate the problems before these countries. Corrupt administrations and numerous revolutions have characterized Central America during the last hundred years so that the progress and development of the countries have been checked. The credit of Central

American Governments has all but been destroyed through default in the payment of debts, debts legally valid but which in some cases were contracted as a result of connivance between officials and foreign promoters so that the funds were dissipated before the people of Central America received much benefit.

Nevertheless, Central American countries are rich in resources, and in natural features and in other ways are attractive. If stability of Government can be established these countries will assume a position of greater importance than that which they now have. Also, if suspicions in Central America as to imperialistic intentions on the part of the United States can be allayed, cooperation and the rapid development of the countries may be expected to follow. It is hoped that this book will contribute to a better understanding of the financial problems before Central America.

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September, 1924

JOHN PARKE YOUNG

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Introduction

DESPITE the frequent claims to the contrary that have been made by popular writers as a result of the world's monetary experiences since 1914, monetary science, like any other true science, is a body of fundamental natural laws. These laws being psychological and social and finding their expression in the activities of man—nature's most complex product—are more complicated in their inter-relationship than are the laws of the so-called natural sciences, and therefore more difficult to disentangle and understand. None the less, in fundamental character the laws of monetary science are no less natural and no less immutable than are the laws of physics or biology. Furthermore, they are fundamentally the same in their applications to all races of people and for all stages of civilization.

Because of their great complexities and of their intimate relationship to human welfare, monetary phenomena do not subject themselves to study by the laboratory method, according to which phenomena under investigation can be more or less isolated, and can be manipulated to suit the purposes of the investigator. If the student of monetary problems could only follow the practice of the chemist and isolate his phenomena, reduce them to simple terms, and then manipulate them to suit the purposes of his investigation, we could make much more rapid progress in our understanding of the laws of money and credit.

One of the nearest approaches that can be made by students of monetary science to the advantages of the laboratory method of study is to be found in the study of currency reforms in small countries whose economic life is simple. For the purpose of the investigator, it is particularly helpful if the currency reforms being

studied in such countries are being pushed through rapidly, so that the forces at work and their results stand out plainly. Herein lies one of the principal services rendered by the present book. Central American republics are all small. Their combined area is only about two thirds that of the State of Texas, and their total population is only about five million persons. Their economic life is simple. Each of the five Central American republics underwent a number of monetary reforms during the time covered by Dr. Young's study; but the period stressed by the book is the war and post-war period, when the monetary system of each of the republics was greatly disturbed by powerful outside economic forces and when, as a consequence, the movements that took place were writ large. The ten year period, 1914-1923, in Central America was therefore particularly favorable for the study of the operations of fundamental monetary laws under simple conditions.

Furthermore, the monetary experience of the different countries studied were widely different. In Guatemala, for example, we see a silver standard country degenerating into a paper money standard, in which the paper is issued almost entirely by a group of commercial banks, and in which the monetary unit depreciates continually over a period of years until it reaches a value equal to only about two per cent of its original gold value. In Salvador we find since the outbreak of the World War a movement from the silver standard to a paper money standard and thence to a gold standard, accompanied by a skillful exchange of the country's old silver in the world's market at the time when high war-time prices for silver prevailed. In Honduras we see an interesting and illuminating experience with a dual currency—a silver standard and a gold standard—in operation at one and the same time within the limits of a country having an area of only about that of the State of Pennsylvania. Nicaragua exhibits some useful lessons in the

operation of Gresham's Law. Here, for example, we find one kind of inconvertible paper money driving out of circulation not only metallic money but other kinds of inconvertible money in certain parts of the country, while in other parts silver coins continue to circulate, and successfully resist the onslaughts of the cheaper paper money. We find in recent years a gold exchange standard built up under American influences and successfully functioning, then suspended under war pressure, and now with difficulty working its way back towards normal. Here also we find an example of a deliberate reduction of the monetary supply with the purpose and result of greatly increasing the gold value of the monetary unit until a predetermined value is attained. Costa Rica adopted the gold standard between 1896 and 1900 by a unique method of issuing gold certificates in return for deposits of gold, but making these certificates redeemable at first only in silver and later, after sufficient gold had been accumulated, of making them redeemable in gold. Here likewise are found some useful lessons in the working of Gresham's Law.

Dr. Young's book is not only valuable because of the light it throws upon some of the natural laws of money. It is also valuable because it provides for the foreign business man, investor and traveller who may be interested in Central America, useful descriptions—heretofore unavailable—of the present currency and banking systems of these countries. Central America is rich in resources of kinds that the world is demanding in increasing quantities—coffee, tropical fruits, cattle and timber. Her five republics are located very near to the United States. Her trade is predominantly with North America and that trade is increasing. To most Americans the Central American republics are practically unknown countries, and this is particularly true of Central American finances. Dr. Young's book offers an interestingly written and

thoroughly scientific account of the monetary experiences of these countries during recent times.

EDWIN WALTER KEMMERER

Princeton New Jersey
May 29, 1924

Chapter I

CENTRAL AMERICA, GENERAL SURVEY

THE five countries of Central America, Guatemala, Salvador, Honduras, Nicaragua and Costa Rica, secured their independence from Spain in 1821, and for a short time after this date were united as a single state. Almost from the first, however, the new state was disturbed by political unrest, so that several revolutions resulted, and the federation lasted only a few years. The local governments came to disregard the central government and the union gradually fell to pieces after a few years of turbulent existence.

From that time to the present the countries have existed as independent republics, although repeated efforts have been made to reestablish the federal union. The political groups in power in the different republics have been unwilling to relinquish their authority, and the five republics have had separate, although not entirely dissimilar histories. The Republic of Panama is geographically a part of Central America, but until recently it has belonged to Colombia and its history is more closely related to that of South America than to that of Central America.

Although the governments of Central America are nominally republican in form, in actuality they have usually been little more than military dictatorships. Elections are held but they are usually only a formality and controlled by the administration. Genuinely free elections have been very rare. Changes in administration ordinarily are accomplished by revolution, consequently the government in power must continually be on its guard against conspiring opponents. The promise of a lucrative job at home or abroad at-

tracts individuals to a revolutionary movement that appears to have a chance of success. The government in office must be generous to its friends and be careful not to create too many enemies if it desires to remain in power. This fact is often a handicap to a well-meaning and honest president, and prevents the adoption of needed reforms or the bolstering up of a bankrupt treasury.

The political history of Central America is chiefly an account of one revolution after another; and of the efforts of the different groups to place themselves in power, or of the ruling party to put its friends in power in a neighboring republic. While revolutions are frequent, the majority of the people take little active part in the disturbances. Contrary to the general opinion in the United States the bulk of the Central American people are of a peaceful disposition and desire only to be left alone to follow their pursuits without interference from marauding revolutionary armies, which take whatever provisions and live stock the peasants may have in their possession.

The majority of the people are unable to read or write and take little interest in governmental affairs. Thus the restraining influence of public opinion has little force, so that official corruption has become a commonplace and is carried on more or less openly. Conditions are worse in this respect in some of the countries than in other countries. Similarly as regards such matters as sanitation, education, or revolutionary disturbances the countries are not all alike. Costa Rica has had a more tranquil existence and in many ways is more advanced than some of the other countries. Much of that which is said above does not apply in the case of Costa Rica.

Geographically and climatically Central America offers a variety of conditions. On the Pacific side of the country is a range of mountains which slope off gradually toward the lowlands along the Caribbean Sea. In the low territory the tropical heat is oppres-

sive but at the higher altitudes the heat is moderated and the climate is favorable to health and to agriculture. Most of the people live at the higher altitudes in the Pacific half of the country. In the low land along the Caribbean Sea bananas thrive, while on the higher plateaus coffee is the chief crop of commerce. The population of the five countries in 1923 was approximately as follows:

Costa Rica	500,000	Nicaragua	650,000
Guatemala	2,180,000	Salvador	1,500,000
Honduras	640,000		

The people of Central America are largely of Indian descent; they are either pure blooded Indians or have an admixture of Spanish blood. There is also a certain amount of negro blood in Central America, especially along the Caribbean coast. In Costa Rica Spanish blood predominates and the people are of a white complexion. Due partly to this Costa Rica has had a somewhat different development than the other Central American countries; she has enjoyed a more stable government and has made greater progress. In Guatemala the Indian continues as a distinct type. There the bulk of the population consists of pure blooded Indians many of whom do not even speak the Spanish language. They live a simple life and have retained many of their original customs which antedate the Spanish Conquistadores. However, in Guatemala as in the other countries the small ruling class is composed chiefly of people of Spanish ancestry. In Honduras, Nicaragua and Salvador the people are mostly a mixture of Indian and Spanish, Spanish blood predominating in the ruling class.

When the Spaniards came to Central America the Indians were subjugated and made to do the hard work. Blended with Spanish stock they now live a primitive life cultivating the land or working as laborers in the towns. They are free laborers except in Guatemala where the peonage system on the large plantations is similar in

practice to a system of slavery. The life of the Central American is simple; his food is chiefly corn in the form of tortillas, beans and rice. Water must usually be carried from a distance and is borne on the heads of women.

A large percentage of the people of Central America are uneducated and know very little of what happens beyond their immediate horizon. Educational facilities are extremely meager and lacking entirely to a large proportion of the population. The people have little opportunity to better their condition, and also little ambition to do so. Sanitary and moral conditions are bad, although the Rockefeller Foundation has recently accomplished much in the matter of hygiene, and has practically eradicated yellow fever. To what extent the backwardness of Central America is due to the tropical environment, or to inherent physical qualities of the people, or to political and social factors admits of considerable speculation.

The continual turmoil which has existed in Central America for the past one hundred years has not been conducive to the development of sound principles of government finance. The motive of governing officials has too often been to secure as large personal profits as possible while in power. Foreign borrowing, at exorbitant terms, and the debasement of the currency have been undertaken as means of increasing the revenue. Reform measures and strict control of moneys coming into and going out of the treasury have often not been desired since a loose administration better served the purpose of the party in power.

Budgets are regularly adopted by the various Governments but are rarely adhered to strictly. The revenues if properly administered would be ample to provide for the ordinary needs of government and leave a surplus for public improvements. Yet government salaries are usually in arrears and the treasuries usually empty. Numerous leakages occur and pay-rolls, especially in the army, are

often padded. Illegitimate claims are often met promptly while legitimate claims and salaries go unpaid; salaries of school teachers are commonly the last to be paid.

The expense of revolutions, and the costs of maintaining armies, have been no small burden upon the treasuries, and have prevented the accumulation of funds for public improvements and other desirable purposes. The armies are a great source of expense and reform here is urgently needed. The armies are used chiefly for internal purposes, to put down uprisings against the Government, and for the distribution of patronage and graft, and in most cases are poorly disciplined and inefficient. The Washington Conventions of February 1923 endeavored among other things to secure reform in the matter of reduction of armaments and the avoidance of revolutions; however it does not appear that the results will be as far-reaching as was originally hoped.

Each of the five countries has a foreign debt on which the interest is either now in arrears or has been in recent years. The largest debt is owed by Honduras. It was contracted in London and Paris in 1867-1870 for the purpose of constructing a transcontinental railway. The bulk of the money received from those who bought the bonds was divided between the promoters and officials so that Honduras only built between fifty and sixty miles of railroad, but is burdened with a debt the face value of which, including unpaid interest, in 1923 amounted to about one hundred and forty million dollars. Honduras at the present time is the only Central American country which has not made some adjustment of its foreign debt. Various attempts at settlement have been made but none have been successful. An arrangement favorable to Honduras was nearly consummated in 1923, but was not approved by the Honduran Assembly of that year.

Nicaragua has had a sound financial administration since 1911,

when the country was in such a state of turmoil that the United States intervened. Funds were advanced to Nicaragua by New York bankers, and a complete reorganization of the country's currency and finance has been accomplished. Nicaragua had no credit in the money markets of the world and in order to insure payment of the bonds which were issued, a collectorship of the customs was established. An American collects the custom revenues and before turning over the money to the Government of Nicaragua takes out the amount necessary for the service of the country's foreign obligations.

The relations between Nicaragua and the United States have been the subject of much discussion and criticism, and many individuals look upon the policy of the United States towards Nicaragua as part of a program of general expansion and absorption of countries to the south. A legation guard of American marines has been stationed in the capital of Nicaragua since the latter part of 1912 when a revolution threatened a return to the chaotic conditions of a short time previously, and would have brought an end to the reforms which were just being instituted. About 100 marines are maintained in Nicaragua, which is a sufficient number to inspire order.

The charges made against the United States of interfering in an independent country, aggression south of the Rio Grande, or "Yankee Imperialism" as it is called, are heard throughout all Latin America, and a certain amount of evidence is adduced which appears to support them. Instances cited of American expansion at the expense of Spanish peoples are Texas, California, Cuba and Panama; and now it is charged that the independence of Nicaragua has disappeared. Other countries have felt pressure from the United States in their affairs so that the Monroe Doctrine has often been looked upon as a doctrine of aggression. This view was

strengthened when at the recent Pan-American conference the United States elected not to permit South American countries to participate in the interpretation of the doctrine, but retained it as a national policy to be interpreted by the United States.

The Monroe Doctrine for some time has been unpopular with Latin American countries, as menacing or restraining their independent existence. The doctrine was originally adopted by the United States in the interests of the security of the country against conspiring governments of Europe. It was a policy of self interest, yet at the same time was in the interests of the other American republics; and had it not been for the Monroe Doctrine and the firm stand taken by the United States, the South American countries would doubtless today have been provinces of European nations, as the continent of Africa and other parts of the world have been divided up.

In his speech before the American Bar Association in Minneapolis in 1923 Secretary Hughes said that the declaration by the United States to oppose what was inimical to its safety did not imply an attempt to establish a protectorate. He disclaimed emphatically implications that the United States claimed to superintend affairs in Latin American republics, saying that such implications found no sanction in the Monroe Doctrine. He also declared that the actions of the United States in this hemisphere were not limited by the Monroe Doctrine, but may be determined on grounds of international right and national security. In a later speech in Philadelphia he said that the United States is not seeking economic advantages in Latin America denied to other countries.

When the United States intervened in Nicaragua in 1910 and 1911 conditions were intolerably bad. The tyranny and misrule of President Zelaya had become increasingly oppressive, and practices of civilized nations were ignored in spite of protests from outside

countries. Foreign creditors were pressing Nicaragua for a settlement, and if the United States did not intervene to restore respectable government European nations were ready to assume this responsibility. Intervention by European powers in foreign territory has usually meant permanent acquisition of the territory; therefore if the United States desired to maintain the Monroe Doctrine the duty of restoring order in Nicaragua and placing the country in a healthy condition devolved upon the United States.

Since 1912 Nicaragua has been free from serious uprisings and has enjoyed security of property and person together with a stable government, which are essential to the development of the country and to the prosperity and welfare of the people. The Government in Nicaragua is not representative of the people generally, and remains in office chiefly because the United States has been unwilling to countenance a revolution. However, a Government that is really representative of the people in Central America is seldom found. Hostility towards the United States in Nicaragua is kept alive to a large extent by disgruntled politicians, revolutionists and others who find that the elimination of fraud and extortion is not as lucrative to their pocket-books, nor does it yield the power and influence enjoyed under the old system of government by successful revolution.

Economically the system of financial control exercised by the United States over Nicaragua has been successful in that the business and financial conditions within the country are fundamentally sound; although socially there is still much to be desired. The absence of continual revolutions has been a fortunate event for the country. Revolutions discourage the accumulation of property since there is no assurance that property saved will not be plundered or confiscated without restitution.

Any faults that may be charged against the American administration in Nicaragua appear of small consequence in contrast to

the grave abuses that occurred during the previous years of Zelaya's tyrannical rule. There is undoubtedly more real freedom and happiness at the present time than formerly. A majority of the Nicaraguans are probably satisfied with American control and would resent a return to the old order. They are now enabled to follow their different pursuits without interference from the uncertainties and destruction of revolutions, and the arbitrary measures of government officials. Also most Nicaraguans have little interest as to what goes on within the Government, and are content if left alone and if the Government provides music in the plaza two or three nights a week.

On the other hand, to a certain number of Central Americans interference by the United States is genuinely offensive and seems to menace nationalistic aspirations and the realization of the Central American Union. The Latin American is temperamentally different from the North American and dislikes the seeming bruskness and blunt ways of the latter. People from the United States often appear to be blustering money seekers, and the Latin American resents intrusion in his home country by Americans or any one else. In the relations between the United States and Latin America unfortunate events have occurred and needless irritation has been produced, much of which might have been avoided by a more intelligent appreciation of the Latin American viewpoint.

A strong anti-American sentiment throughout nearly all Latin America must now be overcome, and to an encouraging extent is being overcome. In the Caribbean countries, where the influence of the United States has been especially pronounced, suspicions as to the designs of the United States have been a hindrance to full cooperation between the United States and these countries. Unfounded rumors and misinterpreted facts have done much to impugn the motives of the United States. That the United States has territorial aspirations southward does not need much refutation in

the United States, yet in Latin America it is considered an established fact.

The recent policy of the American Government, in requesting that contemplated flotations of foreign loans in the United States be first taken up with the State Department, gives countries such as those of Central America a certain amount of protection against excessively onerous or unsound arrangements, and against possibly undesirable political features that might be embodied. The policy of the State Department according to Secretary Hughes is "to throw its influence against unfairness and imposition."

The economic penetration by the United States of the countries to the south can not be denied. Economic relations between the United States and these countries are continually becoming more intimate, and a large amount of American capital is invested in Latin America. The United States, however, has not sought special or exclusive privileges in trade or investment, and the intimate relations are the result of propinquity and natural forces.

The interests of Americans and other foreigners in those countries have become extensive, and in the long run if intervention by European powers on plausible grounds is to be avoided, the United States must contemplate the possibility of having to assume the obligation of maintaining reasonable order and protecting the interests of all foreign nationals. Until these countries are able to provide against the excesses which have occurred at various times in the past, the United States, which occupies a peculiar position in relation to Latin America, may have occasion to intervene. In referring to Santo Domingo Secretary Hughes said: "The United States intervened in the interest of peace and order and when these are assured it is not only willing but glad to withdraw."[1]

[1] Hughes, Charles E., *Observations on the Monroe Doctrine*, Government Printing Office, Washington, D.C., 1923.

Chapter II

EARLY MONETARY HISTORY

1. *Spanish period in Central America*

WHEN Central America was a dependency of Spain the country was divided into several separate states which together made up the Viceroyalty of Guatemala, ruled over by the Governor-General residing in the city of Guatemala. The history of the province dates back to the year 1523 when Cortez, after inviting submission from the inhabitants of the country, sent Pedro de Alvarado to enforce submission. Alvarado founded the city of Guatemala in 1524 and three years later received a commission from Charles V, appointing him Governor and Captain-General of the new kingdom.

About this same time Francisco Fernández de Córdoba penetrated into Nicaragua and established settlements there. In 1542 the various scattered settlements throughout the peninsula were united by royal decree under one government, and all came to be ruled from the city of Guatemala. The site of the city was twice moved due to earthquakes and volcanic eruptions, and the present city dates from the year 1777. It has a long history as capital of the province of Guatemala, the province during the Spanish period including the country now covered more or less by the five Central American Republics.

Guatemala was a dependency of the Spanish crown, and like the other Spanish possessions in the New World, soon came to have the Spanish system of currency. However, Spanish currency was not used exclusively, and except in the more important towns, trade during the early period was carried on by means of barter and by means of the native forms of money. The native money consisted

of articles of trade which had come to pass commonly as money. These articles were chiefly maize, which was one of the main items of food, and cacao beans, from which cocoa is made. In some sections cocoanuts passed currently. Cacao beans were a generally recognized form of money and date back for several centuries prior to the coming of the Spaniards. They were probably used as money during the period of the Maya civilization, the ancient ruins of which are still in evidence.[1] Accounts of travellers differ as to the monetary value of the cacao beans during the Spanish period, but the beans appear to have been used chiefly as fractional money and circulated at rates which varied from time to time.

The Spanish system of currency which was transplanted to the American continents was based upon the real as a unit. The real dates from 1369 and was a mixture of silver and copper.[2] It was divided into thirty-four maravedí, which were small coins for minor transactions. Under the Spanish laws of 1497 silver pieces of eight reales were coined, which later came to be known variously as pesos, duros, duros fuertes, or pieces of eight. These silver pieces originally contained 423.716 grains troy, 930.55 fine, which would give them a pure silver content of about 394.829 grains. However, the amount of silver in the peso was reduced at different times, and a mint test in 1626 indicated that it contained only about 386 grains of pure silver. Later tests showed still smaller amounts, and by 1800 they contained only about 371 grains on the average. The reales were also often debased so that the pieces of eight were not always rated as the equivalent of eight reales. The Spanish mone-

[1] The Maya civilization was divided into two main periods and dates back originally to several centuries before Christ. The Maya were perhaps the most highly civilized people of the American continents.

[2] The real was originally 1/70 of a mixture of one marc of silver (3550.16 grains troy) and three marcs of copper.

tary legislation of the seventeenth century was very much confused, indicating a similar condition in the currency. Many of the coins contained was considerably less than that which they were supposed such coins were known as vellón. The coins were clipped, plugged, or impaired in other ways so that the silver which they actually contained a large percentage of copper mixed with the silver, and to contain.

In addition to the silver coins, Spanish gold coins were brought over to America. The common gold coin was the onza. The onza, as its name implies, was supposed to contain about an ounce of gold, but in practice this was not the case. The onzas with which the American colonies were familiar appear to have contained about twenty-seven grams of gold gross,[3] and circulated as the equivalent of about sixteen silver pesos. According to Spanish records they were coined first in 1615 by Phillip III. Another familiar gold coin was the doblón, or doubloon, as it is often called. It was of various denominations and was coined in multiples of the escudo, especially in the denominations of two, four, and eight escudos. These were known respectively as "doblones de á dos," "doblones de á cuatro," and "doblones de á ocho." In America the onza was frequently known as a doblón.

Due to the lack of facilities for coining money in America, in the early part of the Spanish period, nearly all the silver and gold taken from the mines was sent to Spain, and a portion returned in the form of coin. However, as the amount of the metals taken from the mines increased, there were not sufficient coins locally for the purpose of trade, due doubtless to the cheapening of the metals in the neighborhood of the mines as their quantity became greatly increased. The metals themselves came to be used in crude form as money.

[3] An ounce troy is the equivalent of about 31.1 grams.

The result of this situation was the appearance about 1600 of pieces of silver of irregular shapes and bearing the official stamp. These peculiar coins circulated as money and were known as "macacas," "moneda cortada," or sometimes "macuquina." They contained good metal and were made in almost all the customary denominations, usually of silver but sometimes of gold. Although mints existed in America, they were not sufficiently equipped to supply the needs for currency with round money and consequently turned out macacas. The coins were made with Spanish dies and thus had the Spanish insignia. The dies were intended for striking round currency, but the macacas were allowed to take whatever shape resulted when the die was pressed down. The coins frequently had large cracks received in the minting, and the Spanish insignia was often illegible. Macacas were put out by the mints of Peru, Mexico, Guatemala and Spain, but the majority came from Mexico and Peru. The mints in America also turned out a considerable amount of coins of more regular shape, which circulated along side of the macacas.

Macacas were minted in large amounts and circulated widely during a long period of years. It was not until 1873 that their circulation was prohibited in Guatemala, and it was still more recently that they disappeared from circulation in some of the outlying sections of Central America. At the present time they can frequently be found strung as a necklace around the neck of some Indian, and very much cherished. The unsatisfactory nature of macacas as money is apparent since their crude and irregular shape made clipping, and the removing of part of the metal in other ways, comparatively simple. It is not surprising to find that they were the source of much confusion, and when taken in large quantities were accepted by weight, rather than according to their nominal value.

Mints were established early in Mexico and Peru, and in 1733

the Royal Mint in Guatemala was founded. The founding of the mint was an event of great importance and was the occasion for much celebration and ceremony. The dies and special machinery for coinage were brought down from Mexico, and when news arrived that the equipment was in the neighborhood of Guatemala City, the officials and notables of the town went out to meet it. They found it already escorted by men from the neighboring towns, so a procession was formed and the whole entered the city with pomp and ceremony, escorted by a detachment of cavalry. The bells of the city rang and guns fired salutes. It was found that the equipment was coming in two consignments, so when the second consignment arrived a similar welcome was necessary. Then when the first coins were struck there was occasion for another celebration. The chief officials, both civil and clerical, were present at the coining, and after five coins had been struck the party proceeded to the cathedral where a Te Deum was sung. This was followed by a general celebration and fiesta in which all the population participated.

The coinings by the mints in America were not always uniform as regards metallic contents, and coins of inferior weights were frequently struck. Many of the gold onzas were light weight, and consequently did not pass as the equivalent of sixteen silver pesos. The pesos were also often underweight, as were many of the other coins, which fact contributed to the complexities of the currency situation. Coins of American mints even circulated in Europe, both the debased coins and the full weight ones. In 1650 Spain ordered that all the Peruvian coins in the country be taken to the mint and reminted; they were denied currency in Spain. Three years later, in 1653, new coins of Peru were approved and allowed to circulate in Spain.

It can be seen that the currency situation in Spanish-America during the Spanish period was not satisfactory; it was disordered

and full of confusion. The coins in circulation in Central America were a mixed lot of coins from various Spanish-American countries, as well as coins from Spain and other European countries. Combined with these were the rudely minted macacas, which formed an important part of the circulating medium. The coins of similar denominations were often not uniform as regards metallic content, due both to their original debasement and to their later physical impairment. New and full weight coins, if put into circulation tended to disappear, in accord with Gresham's law. Although some of the coins of similar denominations varied widely in contents, most of them were not so far apart but that they passed more or less at a parity in spite of the differences. A person would not hesitate to accept a light weight coin if he knew he could pass it on at the same value for which he received it.

2. *National period*

WHEN Guatemala was under the Spanish crown, domestic affairs ran along without much disturbance. One Governor succeeded another in tranquil succession, a contrast to the events of the past one hundred years. However, about the beginning of the nineteenth century a change took place, when nearly all of the Latin-American states became involved in wars of separation from Spain.

The Royalist Governor of Guatemala, Don Gaviano Gainza, saw the trend of events and adapted himself to the situation, so that Central America came into independence with almost no disturbance. The Governor and other important men of Guatemala City, including both the civil and ecclesiastical, met in conference to decide what course Guatemala should pursue. After lengthy and spirited debate independence was decided upon, and on September 15, 1821, the declaration was signed and indepen-

dence proclaimed. Recognition was accorded by the United States in 1824. Spain at the time was engaged in a more important struggle with the provinces in South America, and was not able to offer any armed resistance to the action of the Central American province.

This marks the beginnings of Central American federation, when all the countries were united under one government. At this time it was assumed as a matter of course that the states would remain together as a single republic. In fact under the new status there was little change in the Government from what it had been before. The Royalist Governor Gainza was retained as head of the independent state, and similarly the local Governors of Salvador, Honduras, Nicaragua, and Costa Rica were retained in office.

However, there was little cohesion in the new state since means of transportation and communication were poor. With the new spirit which had grown up of freedom from restraining authority, hostility between the federal officials and state officials developed almost from the first. The different states respected instructions from the Government in Guatemala only when they chose to do so. Rivalry and dissension soon set in among the states themselves, and among aspiring leaders, so that the union gradually fell apart. A series of revolutions followed by counter-revolutions disturbed the country as different groups tried to assume the power. Morazán of Honduras was the last President of the Federation, and exercised considerable authority for a time. The support given him by the various states soon fell away, and as they turned against him he was overthrown and forced to leave the country. The central government had less and less real authority, and the last federal congress before it adjourned in 1838 declared that the states might govern themselves as they saw fit.

The question of a federal union was complicated—and still is

for that matter—by questions of personal animosity and ambition, so that many who contributed to the overthrow of the central government were in fact loyal adherents to the idea of federation. Unsuccessful efforts at federation have been made at various times since the dissolution of the first union, but the results have all been short-lived, and the states have existed as independent republics.

During the period of Central American federation the currency was little different from what it had been when the states recognized the authority of Spain. The largest silver coin was the peso. The pesos in circulation varied as regards silver contents, but contained in general between 25 and 26 grams of silver .900 fine. A large number of Mexican pesos circulated throughout Central America, which contained about 27.07 grams of silver with a fineness of about .903. The peso was divided into eight reales, and the small coins were reales or multiples or subdivisions of the real. The gold coins were the onzas and medias onzas. The onza was supposed to be the equivalent of sixteen silver pesos, but did not always circulate as such. The coins which were in circulation were a miscellaneous lot from various countries of the world, principally the Spanish countries of North and South America; along with these were a certain amount of European coins. The mints in Central America struck some coins with the insignia of the new Republic, but with the break-up of the federal government such coinings ceased.

The circulating medium after the dissolution of the union continued the same as it had been previously, in fact remained almost the same down to the end of the nineteenth century. The different countries retained the Spanish system of currency, and with it the coins which were in customary circulation. An acuerdo in Guate-

mala[4] in June 1838 declared that there should be published in all the towns a statement that all legitimate money of the different nations should circulate freely and be accepted by everyone; the old macacas were to be received without discrimination on an equal basis with the other money. Anyone departing from the order was to be punished.

The currency was in a badly confused condition, and frequent laws and decrees were issued dealing with the problem. In 1840 the Government of Guatemala said that it would not receive certain coins of Peru and Bolivia which were badly debased. In 1845 it declared against certain Spanish coins, stating at what rate it would accept them. Tables of official ratings were quite common, listing the various coins and the rate at which they were to be received. In July 1851 money of the United States was officially recognized and declared to be receivable for public dues as well as for private transactions, at the rate of one dollar for one peso, both for United States silver coins and United States gold coins. Numerous laws dealing with monetary matters are found on the statute books of Guatemala, indicating that the condition of the currency was not satisfactory.

The Government of Guatemala, as well as of the other states, frequently issued paper notes, which often circulated as money. The notes were usually issued in connection with forced loans, and were acceptable in satisfaction of custom dues and other government payments. They were commonly bought at a large discount. One of the first of these issues was provided for by a decree of 1834

[4] The word Guatemala now ceased to be applied to all the provinces combined, as it had been when they were united under one administration in Guatemala city. After independence from Spain and the dissolution of the federal union, the term was applied specifically to the local territory of Guatemala, exclusive of the four other states, the territory now comprising approximately the present Republic of Guatemala.

when a little over three thousand pesos was offered in the form of prizes to stimulate agriculture within the country.

The condition of the currency in the different Central American countries was very much alike. A traveller through these sections about 1845 wrote the following description of currency conditions:[5]

> The current money of Central America, with the exception of Honduras, is nearly the same as the Spaniards left it, and as all the southern republics in pretending to improve it have only robbed the public by issuing a debased currency, it is fortunate that they left it alone. It consists principally of pieces of silver rudely cut and stamped, of the value of from one half to four reales; it is rather finer than the current hard dollars, but from long use the coins, especially the smaller pieces, have lost a great part of their weight; and I find from examination that one with another they may be said to have lost twenty per cent, eight reales of the current money being one fifth lighter than a new hard dollar, which passes for the same value. . . . All the coins of Mexico pass currently in Central America, and next to the cut silver, form the bulk of the circulating medium; but only the gold ounces and hard dollars of the southern republics are received. The gold ounce—improperly called doubloon in English—weighs 317 grains, and should be exactly twenty-one carats fine. Those of Mexico and Central America, and the old republic of Colombia, are said to be pretty exactly of that fineness, but many of those lately coined by the southern republics have been depreciated; the ounce passes for sixteen dollars in Guatemala and San Salvador, and for seventeen in Nicaragua and Costa Rica, but current silver and hard dollars are generally worth six per cent premium in the latter states, which makes it of actually the same value in them all.

The cheapening of gold due to the increased amount thrown on the market following the California and Australian gold discoveries of 1848 to 1850, caused a change in the market ratio of gold

[5] Dunlop, Robert Glasgow, *Travels in Central America*; Longman, Brown, Green, and Longmans; London, 1847.

to silver, with the result that silver money in Guatemala tended to be withdrawn from circulation. The United States dealt with a similar problem by a law (1853) reducing the amount of silver in the subsidiary coins (coined only on government account thereafter) so that they would remain in circulation. Guatemala endeavored to meet the situation by issuing a decree in 1858 prohibiting the exportation of any silver money or silver bullion. A person leaving the country could take with him only twenty-five pesos in silver money. The situation soon remedied itself since about 1860 the value of gold began to rise, or in other words the gold price of silver began to fall, and the market ratio of the two metals was more nearly what it had been previously.

In June 1869 Guatemala adopted the decimal system as the basis for her currency. This disposition was revised somewhat by a decree in September 1870, which declared that the unit was the peso of 25 grams of silver .900 fine. The peso was considered as divided into one hundred centavos, instead of into eight reales as formerly. The four-real piece would now be the equivalent of the fifty-centavo piece.[6] Instead of the former gold onza equivalent to sixteen pesos, the gold coins were to be in the denominations of five, ten, twenty, etc., pesos. The gold peso was given a weight of 1.612 grams of gold .900 fine. This involved a ratio with silver of about 15.51 to 1, which was close to the market ratio of about 15.57 to 1 at that time. The gold peso thus was given a value close to that of the United States gold dollar which contains approximately 1.672 grams of gold .900 fine. Although gold coins were provided for in the law, the silver peso was made the unit.

The decimal system was not well received by the people generally who were accustomed to the old system of reales, medio reales

[6] The subsidiary silver currency provided in the law was of proportional weight to the peso but was only .835 fine.

and cuartillos, and a decree was issued in December 1871 which rearranged the denominations of some of the smaller coins. This law also increased the weight of the peso from 25 grams gross to 25.40 grams gross. The Guatemalan peso now contained forty centigrams of silver more than the generally accepted pesos of other countries. The result was that Guatemalan pesos began to be exported and replaced by lighter weight ones of Peru and Chile. The coinings at the mint in Guatemala soon began to decline since more pesos could be obtained at other mints for a given amount of silver. From 1859 to 1870 the mint in Guatemala coined about 2,455,000 pesos in silver and about 1,207,000 in gold. After 1870 the coinings were not maintained at this rate. The exportation of the heavier Guatemalan silver and the importation of foreign silver continued, and in 1878 about 321,000 pesos left the country; in 1879 and 1880 combined about 543,000 pesos were shipped out. During these same two years about 1,172,000 pesos in foreign silver were imported.

Coinings of the heavier weight "pesos fuertes" were discontinued in 1878, and in April 1881 a law was approved which provided for the return to the pesos of 25 grams .900 fine, as in the original law. The legal tender quality was also given to foreign silver equivalent or superior in weight to the national money. The foreign coins recognized by the law were as follows: the five-franc pieces of France, Italy, Belgium and Switzerland; the Spanish "peso fuerte"; the pesos of Mexico, Chile, Peru, and Venezuela; and the United States coins of fifty, twenty-five, and ten cents.

The influx of foreign silver money, noted above, appears to have been due to a variety of causes, and not solely to the greater weight of Guatemalan pesos, which were being exported. The reduction in the circulation tended to lower prices, and cause the importation of lighter weight foreign coins, but in addition to this, political

and financial conditions in South America were disturbed at this time. The War of the Pacific between Chile, Bolivia and Peru began in 1879. Peru was experiencing the difficulties of irredeemable paper money. The "billete" circulation increased many fold and in 1879 amounted to about eighty-six million soles. Exchange rates on foreign countries rose and the silver soles began to be driven out of circulation, a large part of them going to Guatemala, and to the other Central American countries where silver still passed currently. A situation existed in Chile similar to that in Peru, and in 1877 the Chamber of Deputies decreed the inconvertibility of the bank notes. Thus Chile went onto the paper basis, which accounted in large part for the exportation of the silver money.

About 1873 the gold price of silver began falling throughout the world. The result was that as the price of silver fell, the mint ratio of the two metals in Guatemala was not in harmony with the market ratio. The gold and silver coins in Guatemala were circulating side by side at their nominal value, which involved the mint ratio of about fifteen and one-half to one, whereas according to the market value of the two metals seventeen or more ounces of silver were needed to be the equivalent of one ounce of gold. The result of this situation was that the gold coins, being undervalued in terms of silver, began to disappear from circulation. Furthermore, the influx of silver coin from South America, and the effect of several of the important countries of the world going onto the gold standard, tended to cheapen further the silver peso in terms of gold. The gold onzas began disappearing about 1875, and by 1878 or 1879 were practically all gone. By this time the smaller gold goins had begun to disappear, so that by 1880 there was practically no gold coin in circulation.

For the next two decades the chief metallic currency in Guatemala was silver money. The coins were a miscellaneous mixture

from various Spanish countries as already noted. The old rudely minted silver macacas or moneda cortada, were demonetized in August 1873, and ordered to be brought to the mint for recoining into Guatemalan currency. They continued to circulate for a short time after this decree, but soon began to disappear and were no longer seen in circulation. The year 1873 thus marks the end of the macacas, a peculiar form of currency which had an existence of about three hundred years, dating back to the early days of the Spanish Conquistadores. Guatemala was the last country formally to declare against these coins, and one of the last countries of the world to have such a primitive form of currency.

After the fall in the gold price of silver and the disappearance of gold coin, the fluctuations in exchange rates in Guatemala upon gold standard countries were more or less in harmony with the fluctuations in the gold price of silver. As the gold price of silver continually fell, exchange rates upon gold standard countries continually rose, as can be seen from the table on page 39. In view of the more recent depreciation of the peso, it is interesting to note that in 1874 and the years immediately preceding, the Guatemalan peso was at a parity with the American dollar.

Chapter III

PAPER MONEY

1. *Silver and paper money on a parity*

THE first bank notes in Guatemala were those of the Banco Nacional de Guatemala, which was founded in March 1874. Funds for the establishment of this bank were provided out of the property confiscated by the Government from the Catholic Church in 1873 following the revolution of 1871.[1] The clergy were strong in Guatemala and were a factor in the political situation. They had accumulated wealth over a period of years and had valuable holdings when their property was confiscated in 1873. They loaned out money, at about six per cent interest, usually on mortgages against farms. The decree of August 1873 which confiscated their property, included all their holdings and property of whatever description.

The Banco Nacional which was founded out of the proceeds of this property was given a capital of two million pesos, which was the estimated value of the confiscated property. The Bank was authorized to do a regular banking business, including that of issuing and circulating bank notes against cash or paper of not more than three months maturity. The notes were legal tender and were guaranteed by the Government. Prior to the establishment of the Banco Nacional in 1874 there were private bankers and merchants in Guatemala who did somewhat of a banking business.

The new government bank had a short existence. In March 1876

[1] The convents of the Church were suppressed a few years after independence was declared in 1821, and the Church never exercised much influence throughout Central America thereafter, except in Guatemala where the orders were restored after the revolution in 1839 when the Conservative party came into power. In Guatemala the Church enjoyed considerable influence for many years and had valuable holdings.

a decree was issued suspending specie payments on the bank's notes, and in November of the same year the bank was ordered liquidated. Its notes passed at a discount for a time, but soon were withdrawn from circulation, and the bank passed out of existence. The following year, 1877, the Banco Internacional was founded. This bank is still in existence and is thus the oldest of the present banks in Guatemala. The Banco Colombiano was founded the following year, 1878, and thus has a history nearly as long. Both these banks were allowed to issue circulating notes. A third bank, the Banco Occidente, was founded a short time later, 1881, at Quezaltenango.

The banks had a little difficulty in 1885 when an army officer approached the Banco Internacional with troops one night, and forced the bank to part with its silver. Thus robbed of its silver reserve, the bank was forced to suspend specie payments. The public was fearful as to the notes of the other banks, the Banco Colombiano and the Banco Occidente, and to alleviate the situation the Government issued a decree, April 6, 1885, declaring that the three banks were not obliged to redeem their notes in gold or silver, and that they might make all payments in their own notes. A decree the following day said that the notes were legal tender for transactions both public and private, the same as coin, "Moneda metálica efectiva." This moratorium on the redemption of bank notes lasted only for about six months, and the notes were then again redeemed in coin. With the exception of this short period the bank notes in Guatemala were continuously redeemable down until 1897 when they became inconvertible and the period of depreciated paper money began.

The metallic circulation from about 1880 onwards consisted chiefly of silver coin; gold had left circulation as already noted, due to the increased value of gold in terms of silver throughout the world. Much of the silver money in Guatemala was in a bad

condition. Many of the coins brought in from other Latin-American states were of inferior weight; and in addition to this Barrios, who was President of Guatemala from 1892 to 1898, coined light weight money, especially in the smaller denominations. A full weight peso, or sol, was melted down, and three or four pesos in light weight coins were made from it.

Issues of paper money by the Government were made at various times, billetes del Tesoro as they were usually called. Several issues were made in 1887 and the years following during the administration of President Barrillas. The notes were redeemable on demand and do not appear to have been the source of much difficulty, although they were not well received by the people. In addition to these were the notes of the different banks, also redeemable on demand.

In 1890 the gold price of silver which had been falling almost continuously for about twenty years, ceased to fall and experienced a marked rise. The result of this was the exportation from Guatemala of a portion of her silver money. The circulation in Guatemala had been increasing for the past decade from importations of foreign silver and from increases in the amount of paper money. When the price of silver rose in foreign markets, it drew from Guatemala a portion of her better silver coins. The increase in paper money also tended to encourage the exportation of silver. To check the exodus of the silver money a law was passed in October 1890, taxing the exportation of silver coin or bullion.

The situation changed very quickly and in 1891 silver was again falling in terms of gold. It fell at an accelerated rate, and instead of silver currency leaving Guatemala it began to flow into the country. It came especially from Chile and Peru, pesos and soles, respectively. The currency came to be made up largely of foreign coins, and in July 1894 the importation of foreign silver was

prohibited. The foreign money in the country was ordered brought to the mint and exchanged for national money.

2. *Inconvertibility of paper money and disappearance of silver money*

THE situation after 1894 again changed its appearance very rapidly, and silver once more began to leave the country. However this time it was not due to a rise in the price of silver abroad. Silver on the contrary continued to fall in terms of gold, and in 1895 averaged about sixty-five cents an ounce as against $1.04 an ounce in 1890, and about $1.32 an ounce in 1872. The exodus of the silver money, beginning in about 1894, was caused by an excessive amount of paper money.

Six banks of issue were operating in Guatemala at this time. These six banks, which are still the only banks of issue, with the years of their founding, are as follows: Banco Internacional, 1877; Banco Colombiano, 1878; Banco Occidente, 1881; Banco Agrícola-Hipotecario, 1894; Banco de Guatemala, 1895; and Banco Americano, 1895. The banks were authorized in their concessions to issue "billetes," redeemable on demand, but which were not legal tender. Billetes were issued from time to time by these banks, beginning in 1877 with the founding of the Banco Internacional, and with a few exceptions were continuously redeemable down to 1897.

Reina Barrios, who became President in 1892, by the only relatively free election ever held in Guatemala, was extravagant in his expenditure of public monies. Although active and industrious, he played havoc with the Government's finances. He borrowed extensively from the banks, which tended to increase the circulation outstanding. As the circulation increased the banks found difficulty in meeting their obligation to redeem the notes in coin.

In May 1897 Barrios borrowed one million and a half pesos

from the banks which was to be used in paying government employees' salaries delinquent for about five months. The loan bore interest at the rate of one per cent a month, and was to be amortized in about one year's time. Coincident with this loan contract a decree was issued, May 21, 1897, relieving the banks of their obligation to maintain payments in current money of gold or silver, "moneda corriente de plata u oro." This moratorium was to last until January 1, 1898, when specie payments were to be resumed. During this period the billetes were declared to be full legal tender in all transactions public and private, and were to be considered the same as metallic money. The Government itself assumed a secondary responsibility for the redemption of these bank notes. This decree marks the beginning of irredeemable paper money with the full legal tender quality, although for a short time prior to this date the notes were in fact irredeemable.

By the end of 1897 the Government had not repaid the money loaned by the banks. Nevertheless a decree was issued, on December 7, which arranged for the gradual redemption of the bank notes. On January 1, 1898, the billetes of one and five pesos denominations were to be redeemable. In March and April other denominations were to be added, and by May 1 full redemption in silver was to be resumed.

When the first of the year came, redemption was attempted but was not long maintained. In February 1898, President Barrios met death by assassination, and Manuel Estrada Cabrera, the first "designado," became President. Cabrera ruled Guatemala with despotic severity for over twenty years, being finally overthrown by the revolution of April 1920.

When Cabrera came into power the treasury was in severe financial straights, and the political situation was disturbed. A new plan of dealing with the paper notes and the Government's debt to the

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banks was evolved by Cabrera and became law in 1898. This plan involved the establishment of a Banking Committee, or "Comité Bancario," as it was known. The Comité was to be composed of a representative of each of the banks which entered into the agreement, and of two representatives of the Government. The purpose of the Comité was to issue billetes to the amount of six million pesos, which were to be used in paying the Government's debt to the banks, and for other Government expenses. The billetes were guaranteed by the Government, and were to be considered the same as coin, "metálico," for the banks as regards redemption of their own notes. Certain governmental revenues were to go to the Comité Bancario to be used in amortizing the billetes it issued and in accumulating a reserve either in gold or silver. When the reserve should amount to thirty per cent the Comité was to begin redeeming the billetes.

Thus a small reserve behind these billetes was expected to support the entire paper circulation, because the banks had the option of redeeming their notes in the billetes of the Comité Bancario instead of in coin. The banks were unable to redeem their notes in coin. The billetes were legal tender, and their payment for all Government and Municipal dues was compulsory, with the proviso, however, that the banks which came into the plan should have their billetes also acceptable for public dues. The banks all came into the arrangement, and agreed to accept the billetes of the Comité as coin in all payments due them. As long as the billetes of the Comité were in existence the banks were not required to redeem their notes in silver. Deposits in metal, however, were payable in metal.

The Comité Bancario was composed of eight members, one from each of the six banks, and two from the Government. However, in practice the Comité was a government body dominated by Cabrera.

It functioned merely as a government institution to issue paper money, and was not in fact representative of the different banks. The billetes were purely fiduciary and were never redeemable in coin. A decree in June 1899 reiterated the fact that the billetes both of the banks and of the Comité were legal tender, and were payable for all obligations even though the contract expressly stipulated that payment was to be made in silver coin.

The banks continued to advance money to the Government, and on August 28, 1899, Cabrera entered into a loan contract with the banks which arranged for the funding of various loans, and provided that the Government should pay interest at the rate of five per cent per annum in "moneda corriente," current money. The contract also arranged for the issuance by the banks of additional amounts of billetes. The certificates of indebtedness which the banks held against the Government were to be considered as valid security to guarantee the notes already in existence and those which might be issued in the future. One of the noteworthy provisions of the contract was contained in article VIII, which declared that the banks were not obliged to redeem their notes in cash, "moneda efectiva," until the Government should have paid in metal, "metálica," the total amount of its debts to the banks, and the billetes of the Comité Bancario.[2] The Government has not yet paid its debts to the banks, and therefore the notes are still inconvertible.

The Banco Colombiano was not a party to this contract. The

[2] This article reads as follows:

"No podrán ser obligados los referidos Bancos al cambio de sus billetes por moneda efectiva, salvo el caso que el Gobierno hubiese pagado en metálico la cantidad total de los créditos de los mismos Bancos contra el Estado y los billetes del Comité Bancario." *Recopilación de las Leyes de Guatemala;* Tomo XVIII, 1889-1900. Artículo. VIII. p. 175.

thirty days allowed by the contract for signing and accepting its terms, were permitted to expire, and the Banco Colombiano negotiated a separate contract under date of November 12, 1900. This contract was similar in its provisions to that negotiated with the other banks, with the exception that whereas in the first contract the Government agreed to pay interest in *moneda corriente*, *current money*, in the contract with the Banco Colombiano these words do not appear. The Government at the present time has not paid the interest on its various loans from the banks, and the Banco Colombiano holds itself to be in a different position from the other banks due to the omission of the above words in the contract; it believes that both the interest and the principal due it are payable in silver money and not in moneda corriente, which for a long time has been paper money.

As the billete circulation increased the silver money began leaving the country. In 1894 the Government looked with disfavor at the large influx of foreign silver and prohibited its importation. However, as the paper circulation expanded the tide quickly turned, and silver began to flow out. The Government now was concerned with keeping the silver in circulation, and took various measures in this endeavor. President Barrios ordered light weight coins struck; a silver sol or peso would be melted down, and four times its amount in inferior coins minted. Some of the smaller coins were only .250 fine, containing three-fourths copper. These coinings were not according to law and were a falsification of the currency. Some of the foreign coins were re-sealed with the Guatemalan stamp on top of the foreign stamp with the hope that this would keep them in the country.[3]

These measures were unavailing, and the silver continued to go

[3] The foreign money recoined in 1898 amounted to 1,080,000 pesos.

out. In the latter part of January 1898, a few days before his assassination, President Barrios prohibited altogether the exportation of silver coin. Nevertheless the silver continued disappearing and in November 1898 Cabrera granted a premium of ten per cent on silver which might be imported.[4] Further coinings of inferior money were made, with a silver fineness of about .500. Finally nickel money was minted.

All these efforts were insufficient to keep the full weight silver in circulation, and by about 1897 or 1898 all except the small silver money and the inferior coins had disappeared, part being exported and part going into hoards. Increased paper money and increased depreciation continued, so that by about 1905 the small and inferior silver coins had also disappeared. Inflation and depreciation continued to such an extent that eventually the copper and nickel coins were driven from circulation. These coins remained in circulation until about 1920. A large number of the copper coins, which were the last to go, were exported to Mexico and Salvador, where in some instances, they were used as tokens by employers to represent a day's work, a meal or whatever was desired.

The following figures on the exportation of silver coins are significant:

1896	*P* 552,203
1897	473,000
1898	22,563

The small amount shown for 1898 is due to the fact that in January of this year the exportation of silver coin was forbidden, and all exportations after this date were clandestine and are not shown in

[4] It was only in 1894 that the importation of foreign silver had been prohibited.

the official figures. Most of the money is listed as going either to the United States or to other Central American States.

COININGS BY THE MINT IN GUATEMALA

1892	P 40,850
1893	339,864
1894	2,061,989
1895	2,245,667
1896	1,252,141
1897	413,267
1898	1,310,000
1900	240,663

(Data taken from Report of the Director of the Mint of Guatemala.)

Chapter IV

PERIOD OF DEPRECIATION

1. *Course of depreciation*

THE Guatemalan peso has been depreciating in terms of gold almost continuously for the past fifty years as a result, first, of the fall in the price of silver beginning about 1873 as we have already noted, and second, of the emission of large amounts of paper money. The regime of inconvertible paper money was started by Barrios in 1897, more or less as a temporary measure with plans for the ultimate restoration of specie payments. Cabrera, who succeeded Barrios in 1898, continued the issuance of paper money as a lucrative source of revenue, and used it in such a way as to preclude any immediate return to specie payments. The paper billetes were not issued directly by Cabrera, but were put out through the Comité Bancario discussed above, to the extent of about six million pesos, and by the banks to a much greater extent in connection with loans to the Government.

Loans by the banks to the Government continued to increase, accompanied by increases in the bank note circulation, and increased depreciation of the peso. The Government would grant authority for a new emission of billetes, usually receiving in return additional credits at the bank. The arrangement was thus profitable for both the Government and the banks. The system, in effect, was not unlike that of pure government fiduciary money, although the notes were issued by the banks and are thus obligations of the banks.

The bank note circulation at the end of 1896 amounted to about ten million pesos. By 1910 this had increased to about seventy-five million pesos, and in 1923 amounted to about three hundred and

seventy million pesos. The banks have participated in this increase in different amounts, the Banco Colombiano having refrained, however, almost entirely from paper issues. The details of this increase in circulation can be seen from the following table.

PAPER CIRCULATION IN GUATEMALA

	SIX BANKS OF ISSUE		COMITÉ BANCARIO	TOTAL
1897	P 10,711,000			P 10,711,000
1898	11,935,000			11,935,000
1899	11,675,000			11,675,000
1900	15,385,000		P 6,000,000	21,385,000
1901	22,481,000		6,000,000	28,481,000
1902	26,033,000		6,000,000	32,033,000
1903	32,651,000		6,000,000	38,651,000
1904	41,782,000		6,000,000	47,782,000
1905	43,914,000		6,000,000	49,914,000
1906	45,649,000		6,000,000	51,649,000
1907	46,849,000		6,000,000	52,849,000
	EMISSION	IN CIRCULATION		
1908	P 57,924,000	P 51,434,000	P 6,000,000	57,434,000
1909	63,588,000	57,140,000	6,000,000	63,140,000
1910	74,708,000	68,271,000	6,000,000	74,271,000
1911	81,189,000	74,543,000	6,000,000	80,543,000
1912	99,981,000	89,092,000	6,000,000	95,092,000
1913	109,647,000	95,739,000	6,000,000	101,739,000
1914	112,074,000	106,425,000	5,782,000	112,207,000
1915	143,079,000	133,776,000	5,782,000	139,558,000
1916	164,910,000	156,819,000	5,682,000	162,501,000
1917	182,300,000	174,935,000	5,604,000	180,539,000
1918	210,238,000	193,072,000	2,879,000	195,951,000
1919	246,058,000	219,718,000	2,126,000	221,844,000
1920	326,436,000	274,847,000		274,847,000[1]
1921	349,076,000	336,109,000		336,109,000[1]
1922	386,054,000	377,230,000		377,230,000[1]
1923	406,741,000	401,306,000	1,047,000[2]	402,353,000

[1] Exclusive of notes of Comité Bancario.

[2] September 1, 1923.

Data taken from Juan María de León, *Contribución y Bases Estadísticas;* from Kemmerer, E. W., *Proposals for Currency Reform in Guatemala,* and from other sources. The figures from 1897 to 1907 represent the total emission of January 1 of each year; those from 1908 to 1923 are as of June 30; those for 1921 and 1922, however, are as of January 1.

It will be noted that the increase in circulation did not cease with the overthrow of Cabrera in April, 1920, but has continued down to the present time.

The billetes of the Comité Bancario have been largely withdrawn from circulation. They were counterfeited to a large extent and like the other billetes, became extremely worn and dirty. In December 1913 about 58,000 pesos of them were incinerated. Incinerations continued so that by the end of 1916 about 395,000 had been destroyed. After this time their destruction ceased, although a large number were withdrawn from circulation, until after Cabrera was deposed. On May 1, 1920, nearly four million of them were incinerated. Others have been destroyed since then so that at the present time only about one million are still in existence.

Behind their paper notes the banks on June 30, 1898, held in their vaults metallic currency to the extent of about 2,800,000 pesos. By June 30, 1899, this had declined to about 1,750,000 pesos. and on January 1, 1921, amounted to only about 324,000 pesos. The circulation on the latter date was about 356,000,000 pesos, and the metallic reserve thus less than one tenth of one per cent, a negligible amount.[8] The asset behind the billetes is chiefly the debt of the government to the banks.

The gold value of the Guatemalan peso continued to fall during the long period of increasing paper money, as it fell during the previous period of the declining price of silver. In 1870 the gold value of the peso was approximately equivalent to that of the dollar. By 1895 the price of silver had fallen to such an extent that the

[8] This is estimating the paper peso as the equivalent of the silver peso. If the paper peso has a value of two cents gold, and the silver in the silver peso is worth forty-seven cents in gold (silver at sixty-five cents per ounce troy), the reserve would amount to a fraction over two per cent.

value of the peso was about fifty cents, just half its former value. By 1900, after inconvertible money had come into being, its value was reduced to fifteen or sixteen cents, and by 1905 to five or six cents. In 1921 it was worth between one and a half and two cents, and at the present time, 1924, has about this value. Accompanying this fall in the gold value of the peso has gone a rise in domestic prices and wages, necessitating constant readjustments.

The continued depreciation of the currency has wrought hardships to various classes of individuals. Those who loaned money one year with the peso at a certain value, and received back the money a few years later, when the peso had perhaps one third its former purchasing power, experienced a very real loss. What the creditors lost, of course the debtors gained. Prices of commodities have risen as the paper circulation increased. Since wages, as a rule, move more tardily than general prices, the wage earners in Guatemala during most of the last half century have been continually in the position of trying to catch up with the advancing cost of living, always receiving a little less than their due. This accounts in part for the favor of the present system with the agricultural or employing class.

2. *Foreign trade and exchange rates*

The depreciation in the gold value of the peso is expressed in exchange rates on gold standard countries, and can be seen from the following table and charts.

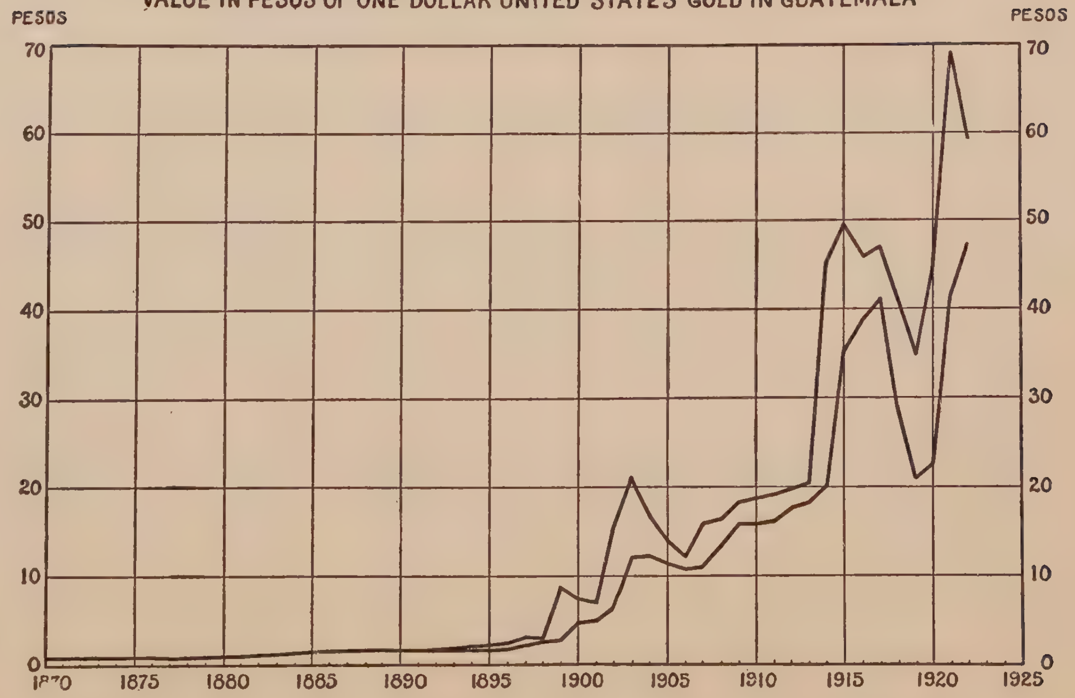
Value in Pesos of One Dollar United States Gold in Guatemala

	Yearly Average		High	Low
1871	*P* 1.00	1896	*P* 2.30	*P* 2.07
1872	1.00	1897	3.12	2.32
1873	1.00	1898	3.00	2.49
1874	1.00	1899	8.50	3.00
1875	1.02	1900	7.50	4.50
1876	1.05	1901	7.26	4.95
1877	1.05	1902	15.00	6.80
1878	1.08	1903	21.00	12.15
1879	1.12	1904	16.90	12.25
1880	1.16	1905	13.60	11.60
1881	1.14	1906	12.00	10.80
1882	1.15	1907	16.05	11.00
1883	1.18	1908	17.40	13.80
1884	1.18	1909	18.50	15.60
1885	1.22	1910	18.50	15.50
1886	1.30	1911	19.30	16.10
1887	1.30	1912	19.65	17.60
1888	1.29	1913	20.50	18.45
1889	1.34	1914	45.00	20.20
1890	1.39	1915	49.85	35.00
1891	1.32	1916	46.00	38.70
1892	1.53	1917	42.00	36.45
1893	1.78	1918	41.00	29.70
1894	1.90	1919	35.00	21.00
1895	2.00	1920	45.65	22.25
		1921	69.25	41.25
		1922	59.25	47.50

Data from 1871-1895 furnished by Julio Samayoa of Guatemala City; from 1896-1922 by Juan María de León, Commission Merchant of Guatemala City.

CHART I

VALUE IN PESOS OF ONE DOLLAR UNITED STATES GOLD IN GUATEMALA



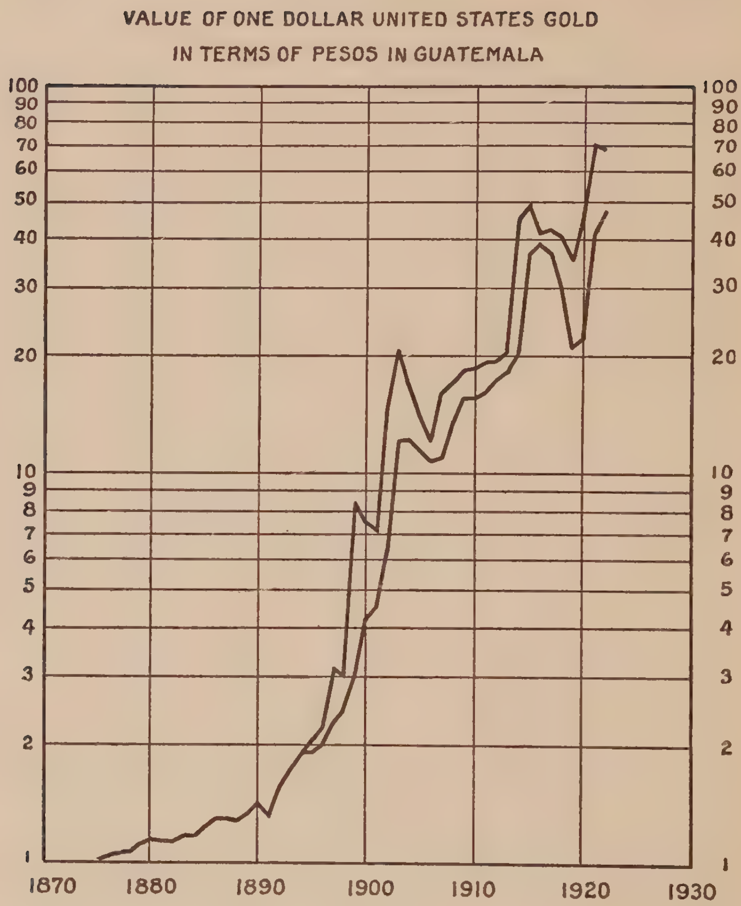
In order to show the relative importance of the early depreciation of the peso, the same data have been plotted on logarithmic scale. The fall in the value of the peso from one peso to the dollar in 1870 to two pesos to the dollar in 1895 is of the same relative importance as the later fall from thirty pesos to the dollar in 1919 to sixty pesos to the dollar in 1921. These two changes are given equal weight on logarithmic scale. A comparison of the two charts shows how on chart I, drawn to arithmetic scale, the gradual halving of the value of the peso from 1870 to 1895 appears as of minor importance, while a similar degree of depreciation from 1913 to 1915 stands out boldly. On chart II (p. 42) these same relative degrees of depreciation are represented as of equal importance.

Since the currency of Guatemala can not be shipped out of the country in payment of international balances, exchange rates fluctuate erratically with the demand and supply of drafts. The extreme nature of the fluctuations within a single year can be seen from the following rates on New York, pesos for one dollar:

	LOW	HIGH
1919	21	35
1920	22	46
1921	41	69
1922	48	59

The continual fluctuations cause obvious evils. Importing merchants selling goods in pesos never know what they will have to pay when purchasing dollars to cover importations of these goods. This element of risk is reflected in higher prices to the consumers. In order to avoid the difficulties consequent upon the fluctuating value of the peso, a large amount of business is being transacted in terms of dollars. Speculation is prevalent and to the extent that it anticipates the fluctuations, its tendency is to equalize the rates.

CHART II


VALUE OF ONE DOLLAR UNITED STATES GOLD
IN TERMS OF PESOS IN GUATEMALA
100
90
80
70
60
50
40
30
20
10
9
8
7
6
5
4
3
2
1
1870
1880
1890
1900
1910
1920
1930

The demand for foreign drafts comes largely from merchants who import various kinds of merchandise and manufactured articles. These articles are principally as follows: cloth of various kinds, miscellaneous food products, iron and steel manufactures, drugs and chemical goods. The larger houses usually buy on open account, while the smaller ones have drafts drawn against them which are either taken up by themselves or by the banks for them.

The supply of bills in Guatemala on foreign countries comes almost entirely from coffee shipments. Thus the fluctuations in the price of bills tend to be influenced by the size of the coffee crop and the price it will bring in foreign markets. Other export products of importance are as follows: bananas, hides, sugar, hard woods, and chicle.

The importations into Guatemala before the war came from the following countries in the order of importance: United States, Germany, England, France, and oriental countries. Since the war Germany has yielded second place to England as shown by the following figures.

SOURCES OF IMPORTS INTO GUATEMALA

	1922	1923
United States	62 per cent	60 per cent
England	15 " "	15 " "
Germany	11 " "	12 " "
Other countries	12 " "	13 " "
	100 " "	100 " "

The principal countries to which exports went before the war were as follows in the order of importance: Germany, United States, England, Austria-Hungary, and Holland. Most of the coffee went to Germany. The effect of the war upon the direction of Guatemala's export trade was to place the United States in the

lead as the chief country for exports, and to increase the importance of Holland, which remained neutral during the war.

Destination of Exports from Guatemala

	1922	1923
United States	67 per cent	77 per cent
Germany	16 " "	14 " "
Holland	9 " "	2 " "
England	2 " "	2 " "
Other countries	6 " "	5 " "
	100 " "	100 " "

German interests in Guatemala before the war were very great. The bulk of the coffee crop was shipped to Germany, and marks were an important currency dealt in on the exchanges. A large amount of German capital was invested in Guatemala, and German mercantile houses there were very strong. When the war started importations from Germany were practically cut off, and the Germans in Guatemala soon found themselves in a very difficult situation. In April 1917 Guatemala broke off relations with Germany, and co-operated with the United States in measures directed against the Central Powers. Property of the Germans in Guatemala was taken over, and the Germans there found their lot a hard one. Many of them turned their property into American money as far as possible and stored it away. Since the war the Germans have regained a portion of the ground lost, and are again playing a prominent part in Guatemalan trade and commerce.

When the European source of supply to the merchants in Guatemala was cut off, they turned to the United States by force of circumstances. As a result, trade with the United States increased greatly, and has remained large. Although European countries have taken back a part of their former trade, the United States has a larger share than formerly. The above percentages show the

present relative importance of the United States in Guatemala's trade, and the following table shows the importance as contrasted with the year 1913.

IMPORTS INTO GUATEMALA

(In terms of United States gold)

	1913	1921	1923
United States	$4,042,000	$6,529,000	$6,520,000
Germany	1,635,000	1,110,000	1,302,000
England	1,291,000	1,898,000	1,666,000
France	322,000	437,000	307,000
Japan and China	244,000	182,000	
Italy	100,000	89,000	
Spain	89,000	117,000	
Other countries	236,000	328,000	1,046,000
Total........	$7,959,000	$10,690,000	$10,841,000

EXPORTS FROM GUATEMALA

(In terms of United States gold)

	1913	1921	1923
Germany	$7,654,000	$1,760,000	$2,048,000
United States	3,923,000	8,110,000	11,331,000
England	1,600,000	136,000	355,000
Austria-Hungary	514,000		
Mexico	78,000	157,000	
Holland	48,000	1,546,000	
Other countries	623,000	422,000	992,000
Total........	$14,440,000	$12,131,000	$14,726,000

Thus from the standpoints of exports and imports the United States is the leading country in Guatemala's foreign trade. Complaints are frequently heard of inferior methods of doing business by Americans, especially as regards terms of credit, filling of orders, and packing of goods. These are common complaints against

Americans, and have been heard in various parts of the world. Although in the past there may have been a basis for complaints, most of the charges are probably now outworn and exaggerated as applied distinctly to American firms. However, the terms of credit extended by the Germans were very liberal in comparison to those of many American houses. Most American drafts have been sight drafts. Interest rates in Guatemala are extremely high, and if an American sight or thirty day bill comes with a shipment of goods, the local merchant must be financed by his home bank, paying high interest charges—twelve to eighteen per cent frequently—until he has disposed of his goods. He much prefers to pay a slightly higher price for his goods, and have sixty or ninety days in which to pay for them.

The importance of the United States as a market, and as a source of purchases for all the Central American countries appears to be permanent, and based upon economic grounds. The proximity of the United States reduces freight charges, and frequent steamship service facilitates intercourse. The demand in the United States for the tropical products of Central America is growing, and on the other hand the products of American factories are finding increasing popularity throughout Central America. The recent increase in the foreign trade of the United States has caused Americans to learn more of foreign trade methods, so that their goods are coming into greater favor.

3. *Coffee industry*

THE coffee industry is the most important industry in Guatemala. Guatemala produces more coffee than any of the other Central American states, and ranks third in the countries of the world, Brazil being first and Colombia second. The Dutch East Indies also produce a large amount of coffee. Coffee in Guatemala is

grown chiefly on the Pacific side of the country, somewhat elevated above the sea level, and is of an especially fine flavor, thus always bringing a good price in the foreign markets. The fruit ripens in the summer months and by November or December has been dried and shipments begun, which continue until about May or June.

Prior to the war Germany received most of Guatemala's coffee. War conditions altered trade routes and markets so that San Francisco now has come to be an important market for Central American coffee. With the other markets of New York and New Orleans, the United States takes the great bulk of Central America's coffee.

The coffee plantations in Guatemala are nearer the Pacific side of the country than the Atlantic side. However, in order to aid the United Fruit Company, which operates a line of vessels out of the Atlantic port of Barrios, freight rates have discriminated against the Pacific ports of San José and Champerico in favor of the Atlantic side. This has affected the amount of coffee shipped to San Francisco. Recent readjustments in rates have tended to reduce this inequality, and with more frequent steamship service on the Pacific side the importance of San Francisco as a coffee market is increasing.[4]

The coffee industry, unlike the banana industry, is to a large extent in the hands of Central Americans. The coffee plantations are usually large, and in Guatemala are owned by a relatively small number of the population, mostly individuals of Spanish descent. However, coffee "fincas" owned by Germans and by Americans are quite common. A large number were originally set out by Germans, or later were acquired from native owners. The plantations are increasingly passing into the hands of foreigners, either

[4] On account of the depreciating value of the paper peso the Government has declared coffee duties payable in gold or the equivalent. Practically all other Government payments are on the paper basis.

through outright purchase or through acquisition under a mortgage.

The work on the plantations is performed chiefly by Indians. They work under the peonage system which in effect is not unsimilar to a system of slavery, and is subject to grave abuses. The Indians contract themselves out to work, receiving a customary advance in money at the time. Once in debt they are under the control of the employer, and since wages are extremely low, find it almost impossible to free themselves from debt. The entire family works, and together get no more than enough to provide the bare necessities of life under an extremely low standard of living. The improvident Indians accept advances in money unmindful of the burdensome terms under which repayment is to be made. The contract labor system is frequently imposed upon laborers by duress, or when the laborer is incompetent to contract freely. The growers provide maintenance for the workers, the food consisting chiefly of corn and beans. Thus the crops of these articles are of importance to the coffee growers.

The number of free laborers who come in to help out at the time of harvest is decreasing, since these have largely been forced into the service through corruption of local officials or ensnared in other ways. The lot of the Indian is a hard one; his living conditions are of the crudest, he is underfed, ill-treated, and as would be expected, inefficient. The Government at various times has taken measures to destroy the abuses, but the pressure in favor of the system has been so great that little has been accomplished in a practical way. The Indian element is very pronounced in Guatemala. A large number of the Indians have not yet assimilated the Spanish language and customs. They live under extremely primitive conditions, and being held in subjection on the plantations have little opportunity to improve their position.

The moving of the coffee crop is generally financed through the local banks or commission houses. These houses, many of which are very strong, conduct both an importing and exporting business. They import a large amount of flour and other food products, also general merchandise; their business is chiefly wholesale. They export coffee, sugar and other products. In addition they deal in foreign exchange, and do somewhat of a general banking business. These houses, together with the banks and the houses which confine their business more exclusively to coffee, advance credits to the coffee growers.

The grower ordinarily borrows in the spring or summer. He may give a mortgage on his finca, or if he is a man of good credit he is merely allowed to draw, up to a certain amount, $10,000 for example. When his crop has been harvested he must sell to the house which financed him. However, if the two can not agree on a price and the grower chooses to sell to another purchaser, he must pay to the house which financed him what is known as a "falsa comisión." This "falsa comisión" is usually about fifty cents a quintal, and thus puts the grower at somewhat of a disadvantage in disposing of his coffee. Very few of the growers finance their own crops. The growers who ship their own coffee usually borrow against it from the banks.

The following table shows the exportations of coffee since 1875.

Coffee Exports from Guatemala

	Quintales		Quintales
1876	207,000	1883	404,000
1877	210,000	1884	371,000
1878	209,000	1885	520,000
1879	252,000	1886	530,000
1880	290,000	1887	479,000
1881	260,000	1888	366,000
1882	312,000	1889	552,000

	QUINTALES		QUINTALES
1890	509,000	1907	956,000
1891	524,000	1908	608,000
1892	492,000	1909	1,163,000
1893	598,000	1910	704,000
1894	614,000	1911	817,000
1895	692,000	1912	751,000
1896	687,000	1913	917,000
1897	755,000	1914	861,000
1898	826,000	1915	795,000
1899	841,000	1916	881,000
1900	730,000	1917	907,000
1901	754,000	1918	783,000
1902	857,000	1919	898,000
1903	631,000	1920	942,000
1904	992,000	1921	939,000
1905	886,000	1922	938,000
1906	936,000	1923	957,000

The cultivation of bananas along the hot Caribbean sea-coast has developed rapidly in Guatemala as in Honduras, Nicaragua, and Costa Rica. The fruit is now cultivated systematically and shipped by fast steamships to New Orleans, New York, and other ports. The industry has thus given the east coast of Central America frequent steamship service to the United States. The banana industry is chiefly in the hands of the United Fruit Company, and since this company represents foreign capital the industry is not of as great importance to the native Guatemaltecans as the value of the exports might indicate. However, a large number of the plantations are in the hands of native owners, who sell the fruit to the Fruit Company at a certain amount per bunch. Railway lines, built especially for the transportation of bananas, have been extended to the capital, so that Guatemala, like Costa Rica, has a trans-continental railway system.

Chapter V

CURRENCY REFORM

1. *Government debt to the banks*

THE question of currency reform in Guatemala is closely bound up with the question of the debt of the Government to the banks. The contract of August 1899 between the banks and the Government provides, among other things, that the banks are not required to redeem their notes in coin, "moneda efectiva," until the Government pays to the banks the total amount of its debts in metal, "metálico."[1] The debt of the Government to the banks has been increasing since the above date by various contracts, and in September 1923 amounted in round numbers to one hundred and thirty-seven million pesos. The Government has not even paid the accruing interest upon this debt. Thus the banks are not obliged to redeem their notes, and not until some settlement of the Government debt is made will the billetes be legally redeemable. Furthermore, the banks at present are unable to redeem the notes since they have almost no specie. The metallic reserve behind the billetes is less than one tenth of one per cent.[2] Most of the banks' assets which are security for the notes are represented by the government debt.

The debt of the Government has been a source of dispute between the banks and the Government for a long time. The dispute has centered around the question of the kind of currency in which the debt is to be paid. The original portion of the debt, contracted before the depreciation had run its course, is commonly accepted as being payable in silver money, since the contract uses the word "metálico." The remainder of the debt is payable in "national

[1] cf. above, p. 31.

[2] See foot-note above, p. 37.

money." The various contracts under which the debt has increased do not specify metal, but merely declare for current money, or national money—moneda corriente, or moneda nacional. The silver debt amounts to a little over five and one half million pesos, and the accrued interest at five per cent now amounts to about eight million pesos. The interest, however, appears to be payable not in silver, but in current money and thus is in the same category with the rest of the Government debt.[3]

The other portion of the debt of the Government to the banks, payable in national money, amounted in the latter part of 1923 with compound interest to about one hundred and twenty-five million pesos.[4] The bulk of this was owing to two banks, about seventy-five millions pesos to the Banco de Guatemala, and about forty-five million pesos to the Banco Occidente. The principal point in controversy is upon what basis this debt should be paid. Payment in silver is not practical, nor just from the standpoint of the Government. It would entail an almost insuperable burden upon the Government, and further than this, the loans from the banks were made at times when the peso was depreciated, and had only a fraction of its original silver value. Thus the Government should not be asked to pay back a peso more valuable than the one it received from the banks in the first instance. Current money during this period has been paper billetes, and the question resolves itself into one of what value to give the peso when computing the total to be paid back by the Government.

A basis which has been recommended as fair, is that the Govern-

[3] The claim that the original debt is payable in silver is based on the use of the word "metálico" in the contract. Some of the opponents of the banks have contended that in view of this the Government could fulfill its legal obligation by paying the banks in copper pesos.

[4] In addition to this, internal loans outstanding in 1923 amounted to about fourteen million pesos; there is also a small floating debt.

ment should pay each debt according to the gold value of the debt at the time it was contracted, as indicated by exchange rates. According to this plan a debt contracted when the exchange rate was twenty pesos to the dollar would be paid back on an equivalent basis, and at a greater value for the peso than a debt contracted when the peso was at a rate of forty to the dollar. This plan would have the early debts paid in silver or the equivalent. A somewhat different plan is to have all the debts liquidated upon the same basis at a chosen rate, such as thirty pesos to the dollar. This has the advantage of simplicity.

Another question in controversy is that of the delinquent interest, whether it should be compounded, and if so whether this should be annually or semi-annually. The contracts do not specify that the interest shall be compounded, but Cabrera recognized such interest. The banks naturally hold that the interest should be compounded, and that this should be semi-annually.

The Banco Colombiano considers itself on a different basis than the other banks. It negotiated a separate contract with the Government in which it left out the words "moneda corriente." This omission is interpreted as meaning that both the interest and principal of the debt are payable in silver, whereas the interest to the other banks is held to be payable in "moneda corriente," which was paper money. The debt owing to the Banco Colombiano is relatively small, and the bank has only a small amount of billetes in circulation. The original issue of this bank was a little over one million pesos. This amount was never increased, but has been gradually reduced so that the amount outstanding at the first of 1923 was only about two hundred and fifty thousand pesos. The total circulation of the country at this time amounted to about three hundred and sixty million pesos. The Banco Colombiano has thus held aloof from the billete system, and is withdrawing its circulation outstand-

ing as much as possible. It desires to have only a small amount of notes in circulation, since it will thus be able to redeem them easily in silver. It declares that the Government debt to it is payable in silver, and that the bank then will stand ready to redeem its notes in silver.

The banks in Guatemala are in a difficult position being weighted down with Government obligations, and other paper which is of doubtful value. They frequently were forced to accommodate customers against their own judgment on the recommendation of Cabrera—the practice of "recomendaciones" as it was known. Cabrera would give letters to his friends addressed to one of the banks, asking that the bank accommodate the individual. Most of the banks did not dare refuse these "recomendaciones." Thus the banks have been injured, and are not entirely responsible for their present position. Furthermore, the depression of 1920 and 1921 imposed a heavy burden upon most of the banks.

In 1919 the Commercial Bank of Spanish America, affiliated with the Anglo-South American Bank, Ltd., established a branch in Guatemala City and has been doing a general banking business, also carrying on operations in coffee. This bank is not a bank of issue and is distinct from the six native banks, which are closely related with the Government's finance. No American bank has yet established a branch in Guatemala, although the matter has come up for consideration at various times.

2. *Efforts toward reform*

In May 1903 Cabrera endeavored to arrange for a metallic reserve behind the billetes, and issued a decree (number 634) which declared that the amount of billetes without metallic guarantee should be limited to the amount then outstanding, and that all future issues should be secured by specie to the extent of ten per

cent the first year, twenty per cent the second year, and thirty per cent the third year. At the time of this decree there were only about thirty million pesos in circulation, as against four hundred million early in 1924. This regulation, however, has not been observed by the banks. Thus the bulk of the present issue has been made without full observance of legal regulations. The decree of May 1903, also, retained the previous provisions that in order to emit new billetes the banks should first obtain the approval of the Government.

Another phase of irregularity in the present issues is that the charters of all the banks, except the Banco Occidente have expired, so that these banks have at present no legal existence. The concessions of the Internacional, Colombiano, and Americano expired together several years ago; then in April 1923 the concessions of the Banco de Guatemala and the Banco Agrícola-Hipotecario expired.[5] Thus the only bank which has the legal right under its charter to issue notes is the Banco de Occidente which was given a concession to last for fifty years, and which fifty years will not expire until 1931. Efforts on the part of the banks at various times to re-charter were not successful, since the Government desired to leave matters indeterminate and more or less flexible until a general banking law could be worked out, and reform instituted.

Agitation for reform has been prevalent in Guatemala for a number of years. Cabrera did not evince much enthusiasm for reform since the billete system was lucrative to himself and to a

[5] The concession to the Banco de Guatemala was to expire at the same time as that granted to the Banco Agrícola-Hipotecario. The concession to the latter bank was granted in April 1893 by decree number 208, and was to last for thirty years. Article 10 declared that if the bank was not founded within one year the concession would expire. Decree 232 in April 1894 extended this period for another year. The bank was finally founded in 1894, but the concession apparently dates from 1893.

large number of his friends. However, he gave serious attention to the problem under pressure from the United States and others, and in the summer of 1919 plans began to take definite shape.

Upon invitation of the Guatemalan Government, Professor E. W. Kemmerer of Princeton University visited Guatemala in 1919 to study monetary conditions and make recommendations for reform. Professor Kemmerer recommended that a gold unit be adopted equal in value to one-third of the United States dollar. The unit was to be divided into 10 pesos, or 100 céntimos, thus making the peso the equivalent of 10 céntimos, and stabilizing it at a value of $3^1/_3$ cents in United States gold, which was its approximate value at that time. The bulk of the currency was to be fiduciary silver maintained at a parity with gold by a gold reserve of at least thirty per cent. Part of this reserve was to be kept abroad, and redemption of the coins to be made in drafts on the fund in accordance with the principles of the gold-exchange standard. Recommendations for the establishment of a National Bank were also made. The bank was to be the fiscal agent of the Government, and was ultimately to have the exclusive right of note issue as the concessions of the other banks expired. The bank was to be a central bank where the other banks might keep a portion of their legal reserves on deposit. Unfortunately, these plans were not adopted.

Had the plans for the introduction of the gold standard and the foundation of a National Bank as formulated by Professor Kemmerer been put into operation, Guatemala would undoubtedly have been spared to a large extent the acute monetary and exchange difficulties which accompanied the period of depression in 1920 and 1921. Program for reform was interrupted in the first part of 1920 by a revolution in which Estrada Cabrera was overthrown. He had ruled Guatemala continuously since the first of 1898 when President Barrios was assassinated.

The administration of Carlos Herrera which came into power in 1920 was favorable to reform and appointed a local finance commission to determine what measures should be undertaken. The commission, of which Julio Samayoa was chairman, worked out a plan somewhat along the lines of the American Federal Reserve System. There was to be a central government institution which would issue notes to the banks in return for certain securities and gold. The notes were to have behind them a gold reserve to the extent of forty per cent so that they might always be redeemable on demand. The old billetes were to be presented in exchange for new notes at a fixed conversion rate.

The question of the rate of conversion was obviously a matter of great importance since it would fix the value of the old billetes. A rate of forty billetes to the dollar was first considered, but as exchange rates rose rapidly and depreciation continued apace a rate of 50 to 1 was contemplated. The higher the rate selected the lower the value that would pertain to the peso and the cheaper would be the reform to the Government. The banks preferred as low a rate as possible since the debt of the Government to the banks would then have a greater value. The relation between the debtor and creditor classes would be affected very materially by the value given the peso. A high value would be to the advantage of the debtor class while a low value would be in the interest of the creditor class.

During the period of rapidly rising exchange rates at the end of 1920 and the first part of 1921 popular agitation for some kind of reform became pronounced, and in April a public demonstration before the National Assembly was organized to obtain relief from the falling value of the peso. A rather hurriedly drawn up project was adopted which authorized the Executive to establish a bank with a minimum capitalization of ten million dollars. The bank

was to enjoy the right of note issue up to three times its paid up capital and surplus, the notes to be guaranteed by a forty per cent reserve in gold and to be redeemed on demand either in sight drafts or American gold.

Nothing came of the above attempts at reform, and in the fall of 1921 President Herrera again took up the question. He decided to bring in foreign experts who would formulate a plan for general reform and supervise its installation. Negotiations for this were nearing completion in the United States and reform might soon have been under way had it not been for a sudden revolution in December 1921, whereby Herrera was removed from office and a new group came into power. The disturbed conditions postponed any immediate prospects of reform.

General Orellana, who became the new President, realized the necessity of a thorough-going reform. He soon took up the question of reform, and commenced negotiations with American bankers for the flotation of a foreign loan, to provide funds to settle the debt with the banks and to institute a comprehensive banking and currency reform. Negotiations were carried on with Blair & Company of New York, and a plan was worked out whereby money would be advanced to Guatemala for the establishment of a National Bank whose currency would replace the present irredeemable billetes, the new notes to be guaranteed by gold and Liberty Bonds or other governmental bonds in the United States. This loan plan was not approved by the Guatemalan national assembly. Professor Kemmerer visited Guatemala again in the summer of 1924 and at the present writing (September 1924) plans for reform are being worked out.

A decree was issued in September 1923 establishing a "Caja Reguladora" to stabilize exchange rates. The Caja was given a directorate of nine members including the Minister of Finance, and

was to buy and sell in paper currency foreign gold drafts. The Caja was to receive the income from an additional coffee export tax of fifty cents a quintal, and if this money were insufficient the Government would provide further funds. An issue of bonds was authorized. Accordingly bonds were issued and are receivable in payment of the additional coffee duty. The rate at which drafts were to be bought and sold was to be determined by the Caja. A rate of about sixty-three pesos to the dollar was selected when operations were first begun. As coffee bills came on the market the Caja was enabled to reduce the rates several pesos to the dollar. In August 1924 the rates were about sixty pesos to the dollar.

The difficulties which complicate the problem of reform are the way in which the currency system is closely tied up with the six banks and with the debt of the Government to these banks; the banks, the currency, and the Government debt are all inter-related. Any reform must involve all these factors. The security behind the bank notes is the Government debt, and not until the Government pays the banks can the banks redeem their billetes. The Government has not sufficient funds to pay the banks, and therefore a foreign loan is almost essential before a satisfactory reform can be accomplished and the currency placed upon a sound basis.

When the question of a foreign loan is broached, investigation shows that Guatemala's record in maintaining payments on her foreign obligations is not especially favorable. From 1825 until 1856 payments on her share of the debt of the Central American Federation were in default. A refunding operation was consummated in 1856 in London, and in 1869 another loan was contracted. Both these loans went into default in 1876 and remained so until 1888 when a consolidation and refunding operation was again accomplished, the creditors accepting a reduction of the interest in arrears. Default again took place in 1894. In the following year a new ar-

rangement was made whereby internal and external obligations were consolidated into a new four per cent bond issue to the extent of £1,600,000. These bonds were guaranteed by an export duty on coffee of $1.50 per quintal, which was not to be altered for a period of ten years. A loan was negotiated the same year with German bankers also based on coffee duties. Contrary to the agreement, the coffee duties were reduced in 1898 and again in 1899. Interest payments were not maintained after 1898 until 1913, when resumption in accord with the arrangements of 1895 was accomplished. Interest payments are now regularly maintained and have not been in default since 1913. The total foreign debt of Guatemala at the close of 1923 amounted to £1,876,000.

In the light of the past record of default, and the scaling down of the debt through conversion operations, involving a loss to creditors, any new loan would have to be secured by adequate guarantees if it wished to find favor with reputable American bankers.

The debt of the Government to the banks in September 1923 amounted to about one hundred and thirty-seven million pesos. This debt would have a gold value of about $2,740,000 computing the peso at the rate of fifty to the dollar. The sterling debt above amounts to about $9,115,000 ($4.86 to the pound), with annual interest charges at the rate of four per cent exclusive of amortization. These two debts plus internal debts to the extent of about fifteen million pesos—$300,000—give Guatemala a total debt of about $12,150,000. The total revenue in 1922 amounted to about three hundred and seven million pesos, or $6,140,000. Thus, with economy in expenditure—more than has been shown in the last two or three years—and stricter financial control, Guatemala

would have a basis for additional borrowing in order to finance a general currency and banking reform. Following are the total revenues and expenditures for recent years.

	REVENUES	EXPENDITURES	DEFICIT	SURPLUS
1910	P 51,571,000	P 45,959,000		P 5,612,000
1911	62,047,000	69,162,000	P 7,115,000	
1912	71,015,000	76,683,000	5,668,000	
1913	83,644,000	46,464,000		37,180,000
1914	82,400,000	48,736,000		33,664,000
1915	85,008,000	67,841,000		17,167,000
1916	134,935,000	91,753,000		43,182,000
1917	135,472,000	131,413,000		4,059,000
1918	110,937,000	77,666,000		33,271,000
1919	127,249,000	101,028,000		26,221,000
1920	168,482,000	195,715,000	27,233,000	
1921	256,262,000	387,365,000	131,103,000	
1922	306,810,000	348,490,000	41,680,000	
1923	385,874,000	396,122,000	10,248,000	

Chapter VI

MONETARY HISTORY PRIOR TO 1914

1. *Silver standard*

EL SALVADOR, prior to 1914, like Honduras was one of the few countries of the world which retained the silver standard. The silver standard had a long history in Salvador. During the period when the country recognized the authority of Spain the chief coin was the Spanish silver peso, divided into eight reales. Along with the Spanish money, coins of various other countries, especially those of Latin-America, were in circulation. In addition to the silver money a certain number of gold coins were also seen, such as the "onza," equivalent to about sixteen silver pesos. Gold coins, however, never circulated very widely and the chief money was silver money.

The currency of Salvador during the Spanish period was similar to that of the other Central American states and was equally confused. The money being a mixed lot from various countries and struck by different mints was not always uniform, and many of the coins were under-weight or debased. The result of such a heterogeneous condition of the currency was that a table of ratings was frequently necessary to determine at what value the coins were to be received. The rudely minted macacas, pieces of silver of odd shapes, were current in Salvador as in the other Central American countries and were an additional source of confusion. They continued in circulation down to a recent date.[1]

When Salvador became independent from Spain in 1821 there was no great change in the currency situation. The Spanish system

[1] A fuller discussion of the currency in Central America during this early period will be found in the section dealing with Guatemala.

remained, and with it the miscellaneous coins which were in circulation. The money was chiefly from Spain, Mexico, Peru and Bolivia. A shortage of small change soon developed in Salvador, and "moneda provisional" was ordered coined at the mint in Guatemala about 1828 and the years following. In 1851 gold money of the United States was declared officially to be legal tender in Salvador.

El Salvador, so far as can be ascertained, had no general monetary law until February 1883, when a detailed law was enacted. This law adopted as the monetary unit the silver peso of 25 grams .900 fine, which was the customary weight for pesos of other countries at this time. Following the lead of other countries Salvador by this same law of 1883 discarded the Spanish system of eight reales to the peso, and adopted the decimal system whereby the peso was divided into one hundred centavos. Instead of eight reales to the peso Salvador now recognized ten reales to the peso, the five-real piece or fifty-centavo piece containing exactly half the silver in the peso. The smaller coins were of proportional weight but only .835 fine, and were therefore coined only on government account.

The law provided for gold coins, the gold peso to weigh 1.6129 grams .900 fine which is a little less than the gold contained in the United States dollar. This gives a ratio with silver of 15½ to 1 although the market ratio at the time was about 18½ to 1. The law thus undervalued gold, and as was to be expected gold coins were not minted.[2]

As regards foreign money, the law declared that the foreign money circulating in the country, which was the chief currency, should continue to be legal money; similarly with regard to foreign money brought in in the future. A table of equivalents was adopted which listed the various foreign coins and the values at which they

[2] A few gold coins were struck in 1892 but did not remain long in circulation.

were to be received as legal money. Coins not mentioned in the table were to enjoy conventional circulation.

Salvador endeavored at various times to establish a mint for the coining of her own money. In 1849 a mint was authorized and a contract arranging for it was signed. However, the plans were not carried out and operations were never undertaken. In 1891 a concession was granted to certain individuals to establish "The Central American Mint Limited" to coin money in accord with the law of 1883 under the supervision of the Government. This company was organized, and operations in the mint were finally begun in the latter part of 1892 when some national money of both gold and silver was struck.

When the price of silver experienced its prolonged fall, beginning about 1873, Salvador followed the lead of other countries, and attempted the introduction of the gold standard. A law to this effect was passed in September 1892. The law declared the monetary unit to be the peso containing 1.612903 grams of gold, similar to the gold coin which had been provided for in the law of 1883. This weight is slightly less than that of the American gold dollar.[3] The silver money was to remain unchanged, the silver peso weighing 25 grams .900 fine. The banks were authorized to issue notes redeemable in gold, either national gold or foreign gold, on demand. The value attaching to foreign gold coins was specified by law, the American dollar having a premium of four per cent. Coincident with this gold standard law, a law was passed, October 1892, which changed the name of the silver peso to that of "Colón" in honor of Christopher Columbus; the four-hundreth anniversary of his discovery of America was being celebrated at this time.

The weights of the coins according to the new gold standard law were similar to those in the law of 1883. This earlier law had

undervalued gold at the time, and since 1883 the market price of silver had been falling continually, so that by 1892 a similar ratio undervalued gold more than ever. Under these circumstances it was not to have been expected that the plan would have been a success, and that gold would have remained long in circulation. Nevertheless, some of the new gold coins were minted, but they were promptly withdrawn from circulation, most of them being exported, since their value as bullion was greater than their value as money. The Government took various measures to sustain the gold standard, and offered a premium of fifteen per cent on all customs payments made in gold, hoping thereby to encourage the circulation of gold.

These efforts to establish the gold standard were unavailing, and silver money continued to be the chief money of the country. If gold was to remain in circulation and constitute the standard metal, the silver money should have been considered fiduciary and, reduced in quantity, made redeemable in gold. A generous gold reserve was needed to redeem freely the silver money, and thus maintain its value at a fixed ratio with that of gold. The large supply of silver money and the small supply of gold money could not be made to circulate together at the mint ratio when the market ratio was so greatly divergent.

Finally, in 1894, all the laws dealing with the gold standard were repealed, and the silver peso was left the unit as before. The silver standard continued until 1914 when inconvertible paper money came into existence and prevailed until the present gold standard was inaugurated early in 1920.

2. *Fall in price of silver, and foreign exchange rates*

THE gold standard law of 1892 was adopted by Salvador, after considerable debate, as a result of the fall in the price of silver in

[3] The American gold dollar contains 1.671812 grams .900 fine.

gold standard countries and the concurrent rise in exchange rates on these countries. The gold standard was expected to relieve Salvador of the instability in the foreign exchanges, and of the difficulties in the currency situation.

The fall in the gold price of silver throughout the world began about 1873 and continued with some reactions until about 1902. The leading countries of the world, together with many smaller ones, were turning to the gold standard, and Salvador in endeavoring to go onto the gold standard was following the general trend of events. The increased demand for gold throughout the world, and the decreased demand for silver, cheapened silver in terms of gold so that silver standard countries such as Salvador experienced difficulties in their foreign exchange rates. Their monetary units depreciated in foreign markets, and exchange rates in Salvador on gold standard countries rose very greatly. Importing merchants found the cost of foreign goods relatively high when they went to purchase foreign currencies with local pesos to pay for the goods.

The fall in the price of silver can be seen from the following table which shows the average price of silver each year since 1870.

PRICE OF SILVER

Average price per fine ounce in New York; 1870-1873 in London reduced to dollars at par of exchange, ounce .1000 fine. Data taken from Annual Reports of the Director of the Mint of the United States.

1871	$1.33	1882	$1.14	1893	$ .78
1872	1.32	1883	1.09	1894	.64
1873	1.30	1884	1.11	1895	.66
1874	1.27	1885	1.06	1896	.68
1875	1.24	1886	1.00	1897	.61
1876	1.15	1887	.98	1898	.59
1877	1.19	1888	.94	1899	.61
1878	1.15	1889	.94	1900	.62
1879	1.12	1890	1.05	1901	.60
1880	1.14	1891	.99	1902	.53
1881	1.13	1892	.88	1903	.54

1904	$ .58	1911	$ .54	1918	$ .98
1905	.61	1912	.62	1919	1.12
1906	.67	1913	.61	1920	1.02
1907	.66	1914	.56	1921	.63
1908	.53	1915	.51	1922	.68
1909	.52	1916	.67	1923	.67
1910	.54	1917	.84		

Since Salvador was on the silver standard exchange rates during this period followed, in general, movements of the price of silver, until 1914 when the war in Europe brought in complicating factors. During the few years following 1890 exchange rates rose especially fast. The table given in Appendix G shows the value in gold of the silver contained in the peso at various prices for an ounce of silver.

The most rapid fall in the price of silver occurred between the years 1890 and 1895. After 1895 the price showed more stability, gradually tending downward however. A recovery took place during 1905, 1906, and 1907, after which the price again fell to its previous low levels. When the war in Europe commenced in 1914 the price of silver at first continued low. However, after 1915 it started to rise rapidly and under pressure of the demand from India and elsewhere mounted until it reached the old prices of fifty years previously. This rise in price, however, was to a large extent merely the depreciation of gold, in terms of which metal the price of silver was quoted.

The exportation of silver money was interfered with by the Government of Salvador at various times. In February 1896 a decree was issued which prohibited the exportation of national and foreign silver for fear that a "lack of change will produce a monetary crisis."[4] This law continued in operation for one year.

[4] Salvador, *Repertorio de Legislación*, 1896.

In March 1899 a tax of thirty per cent was placed upon the exportation of silver money. In order to prevent evasion of this law silver bullion was not allowed to be exported unless it came from the mines. However, enforcement of the law was difficult and evasion apparently took place. To the extent that the law was effectively enforced exchange rates on foreign countries were raised, or were prevented from falling, since the law hindered or made more costly the establishment of balances abroad.

Exchange rates in Salvador, as in Guatemala, are influenced profoundly by the size of the coffee crop and the price it brings abroad. Coffee growing is the chief industry of the country, and shipments of coffee provide the source of most of the foreign drafts. Thus coffee is a dominant factor in the foreign exchanges. When the combination of a good coffee crop and good coffee prices prevails, balances accumulate abroad and exchange rates tend to fall. The country is then fairly prosperous. Buying of foreign goods, which are more or less articles of luxury, takes place, and imports tend to increase.

The following table shows the high and low rate on New York since 1905.

EXCHANGE RATES ON NEW YORK FOR SIGHT DRAFTS IN SALVADOR[5]
(Pesos per 100 dollars)

	HIGH	LOW		HIGH	LOW		HIGH	LOW
1906	237	224	1911	258	244	1916	293	289
1907	262	224	1912	255	229	1917	275	252
1908	269	240	1913	255	231	1918	264	210
1909	285	254	1914	350	228	1919	215	183
1910	303	260	1915	311	229	1920	226	185
						1921	225	199
						1922	210	198.5
						1923	207	199

Rates from 1905-1917 taken from Government reports; 1918-1923 supplied by Banco Occidental.

[5] Also see table on p. 79.

Chapter VII

GOLD STANDARD ESTABLISHED

1. *Banks and bank note circulation*

THE first bank notes in Salvador were those of the Banco Internacional which was founded in 1880, being the first bank in the country. This bank was given the exclusive right to issue notes which were receivable in the public offices. A second bank was founded in 1885, the Banco Particular, and was also given the right to issue notes which were to be receivable in the public offices provided permission were obtained from the Banco Internacional. The Banco Particular was changed in 1892 into the Banco Salvadoreño, which institution exists at the present time under this name. In 1898 the Banco Internacional was merged with the Banco Salvadoreño. Permission was given to the Banco de Nicaragua in 1893 to establish a branch in Salvador. The name of the Nicaraguan bank was later changed to that of London Bank of Central America, Ltd., and in 1902 the branch in Salvador was taken over by the Banco Salvadoreño. Thus the present Banco Salvadoreño is the outgrowth of several banks.

Two other banks of issue exist in Salvador at the present time, the Banco Occidental founded in 1890, and the Banco Agrícola Comercial[1] founded in 1895. There are thus three banks of issue in Salvador. Each of these banks is required to keep a metallic reserve against its notes of at least forty per cent, and a reserve of twenty per cent against sight deposits. The law declares the legal reserve against notes to be fifty per cent, but the concessions of the banks, which antedate the law, specify forty per cent.

[1] The Banco Agrícola Comercial is owned to a large extent by the Anglo South American Bank Ltd.

In addition to these native banks the Commercial Bank of Spanish-America, Ltd., has opened a branch in Salvador. This bank is an English institution affiliated with the Anglo-South American Bank, Ltd. It is not a bank of issue, and confines its operations almost entirely to foreign business. It buys and sells coffee, deals in foreign exchange and does a large collection business. Private bankers, merchants and commission houses also do a considerable banking business in Salvador.

A fourth bank of issue, the Banco Nacional, founded more re-recently than the other banks, became involved in difficulties and failed in November 1913. Its notes immediately went to a discount. The failure of this bank brought the other banks under general suspicion and a run on the various banks for silver money took place. The combined reserves of the banks which amounted to over four and one-half million pesos on June 30, 1913 fell to considerably less than two million pesos by December 31, 1913. The emergency was considered sufficiently serious by the Government so that a six months moratorium, beginning in November 1913, was granted upon the redemption of all bank notes. The banks then proceeded to buy up silver money and replenish their silver reserves so that before the six months expired they were able to resume specie payments.

When the war in Europe commenced in the summer of 1914, Salvador, like most other countries of the world, experienced a financial crisis. The merchants in Salvador were asked by their European creditors to remit funds immediately. The demand for foreign drafts in Salvador was so great that their price rose sharply. The following are the monthly average rates for sight drafts on New York during 1914, pesos for 100 dollars:

1914	January	233	March	229
	February	230	April	239

May	239	September	335
June	242	October	300
July	246	November	300
August	292	December	279

High was 350 September 9.

With exchange rates high the exportation of silver money commenced. A strong demand for silver money was also evidenced on the part of the people generally for the purpose of hoarding. In Central America a large percentage of the people are suspicious of banks (often from sad experience), and prefer to put their savings away in the form of hard money locked up in strong boxes. Thus at the first sign of difficulty the banks are subjected to a drain on their metallic reserves.

During the excitement of the first few days of August 1914 the banks were called upon to pay out large amounts of silver coin. In order to relieve the situation the Government on August 11 issued a decree extending to the three banks of issue a moratorium on the redemption of their notes and the payment of all their other obligations in specie. The moratorium was to last until one year after peace was signed in Europe. Thus the banks were relieved of the obligation of paying out silver money. The banks were ordered to retain in their vaults all the silver money which they then had with the exception of the fractional money which was to be paid out and which would go into general circulation. The decree also established what was known as the Junta de Vigilancia, a joint commission representative of the Government and the banks, which was to see that the dispositions just adopted were properly enforced.[2]

The banks at this time held in their vaults the legal reserve of forty per cent as a guarantee for their circulation. However, it was

[2] A decree of July 1920 arranged for the Junta de Vigilancia to become a permanent body to exercise general supervision over the banks of the country.

sealed under government seal and was not available for use. Under these circumstances the silver money very promptly began to disappear from circulation and soon was at a premium in terms of the paper bank notes. The premium on silver varied from four or five per cent to a maximum of about thirty per cent. The following table shows the paper circulation of Salvador and the metallic reserve behind it.

COMBINED BANK NOTE CIRCULATION OF EL SALVADOR
(December 31 of each year)

		CIRCULATION	METALLIC RESERVE	PER CENT
1908		*P* 3,869,000		137
1909		4,380,000		114
1910		4,847,000		78
1911		5,530,000		84
1912		5,652,000		91
1913	June 30	*P* 6,766,500	*P* 4,690,000	69
	Dec. 31	4,469,100	1,714,900	38
1914	June 30	3,498,300	4,514,800	130
	Dec. 31	6,062,600	3,664,900	60
1915	June 30	7,041,000	3,893,600	55
	Dec. 31	7,903,000	4,444,900	56
1916	June 30	9,246,800	5,101,600	55
	Dec. 31	9,612,000	5,520,900	57
1917	June 30	10,984,700	6,055,500	55
	Dec. 31	11,195,200	6,064,200	54
1918	June 30	12,164,700	6,121,100	50
	Dec. 31	14,183,600	6,622,900	47
1919	June 30	12,802,600	6,463,300	50
	Dec. 31[3]	*C* 14,635,800	*C* 10,690,900	73
1920	June 30	13,849,000	10,265,700	74
	Dec. 31	8,219,400	4,729,400	58
1921	June 30	6,003,100	3,379,600	56
	Dec. 31	7,017,800	4,057,100	58
1922	June 30	7,989,900	4,582,500	57
	Dec. 31	9,381,400	6,290,300	66
1923	Dec. 31	10,166,500	6,674,200	66

[3] After currency reform had been adopted.

The effect of the failure of the Banco Nacional in November 1913 can be seen from the figures for December of that year. The paper circulation at the end of December fell off by over two million pesos as compared with the June figures. The metallic reserve at the same time declined by nearly three million pesos, reducing the reserve to thirty-eight per cent.

During the first six months of 1914 the banks built up their reserves and at the same time contracted their circulation. Thus the war in the middle of 1914 found the banks in an unusually strong position as regards reserve percentages. However the sudden demand for silver, and the expansion of note circulation changed the situation abruptly so that by the end of 1914 the reserve percentage was cut in half. Although the reserve was still ample it remained unused in the vaults of the banks on account of the moratorium which was in effect.

It will be noted that the note circulation showed a steady growth from the middle of 1914 until the first of 1920. The banks were not required to redeem their notes during this period, but they maintained behind the inconvertible paper notes the full legal reserves. The increase in circulation was from three and one half million pesos at the middle of 1914, an unusually small amount, to over fourteen and one half million at the first of 1920, an exceptionally large amount.

2. *Gold standard installed*

The gold price of silver began to rise about 1915 and continued upward until 1920 when it reached peaks it had not touched before for fifty years. In 1915 the silver in the peso was worth about forty cents in American gold. By 1917 it was worth about seventy-five cents and for a while in 1920 was worth a dollar.[4] A large amount

[4] The pesos contained 25 grams of silver .900 fine. (See chart on p. 97.)

of the silver money in Salvador found its way out of the country, attracted by high prices for silver abroad. The rise in the price of silver which was taking place was to a large extent merely the depreciation of gold. Due to the inflation in Europe and the United States gold had become relatively cheap, and its purchasing power less.

When the price of silver was high in 1919 and 1920, or when gold was cheap, was an opportune time for Salvador to sell out her silver currency and replace it with gold. Salvador shrewdly took advantage of this, and by disposing of her silver at a good profit was enabled to establish the gold standard. The actual circulating medium at this time was irredeemable paper bank notes, but a large amount of silver currency was locked up in the vaults of the banks and was lying idle. This silver money was sealed under government seal and the banks were not allowed to divert it to any purpose.

Salvador attempted the introduction of the gold standard, it will be remembered, in 1892, but the plans were not successful and silver money continued to be the currency of the country until after the outbreak of the war in 1914 when the period of inconvertible paper commenced. Special interest in currency reform became evident early in 1919, and in June 1919 the National Assembly passed a law authorizing the President to appoint a Monetary Commission to study the situation and make recommendations for reform. The Commission was instructed to present a project in the form of a law by the first of January 1920. The President was also empowered to invite foreign currency experts to come to Salvador and assist the Monetary Commission, but no such experts were engaged.

The Commission was promptly organized and in two months, August 1919, made a report. Various plans were discussed by the

Commission, and two projects were finally presented for consideration, both involving the adoption of the gold standard. The high prices then prevailing for silver caused events to move rapidly and on September 11, 1919, the National Assembly adopted a law embodying the gold standard.

The gold standard law declared the monetary unit to be the colón weighing .836 grams of gold .900 fine, which makes the colón almost exactly the equivalent of fifty cents in American money.[5] The law demonetized all the old silver money both national and foreign, with the exception of the small coins, twenty centavos and under. All obligations payable in silver pesos were now payable in gold colones at the rate of one peso to the colón. This provision applied also to the bank notes, although they were inconvertible since the moratorium was still in force, and would remain so for several months yet. The banks were ordered within three months time to substitute American gold for the silver reserve which they held. American gold should be first imported before the silver could be released.

The profit derived from the sale of the silver abroad was the subject of some dispute. The question was whether this profit, due to the increased value of the silver, should go to the banks which held the silver, or whether it belonged to the people generally who were not able to draw the silver from the banks since the notes were irredeemable. The Government decided the question by declaring in the law that, after providing for the gold reserve at the rate of one gold colón—fifty cents American gold—for each silver peso held by the banks, half of the net profit derived from the sale of the silver should go to the Government and half to the banks.

A second law, passed the same day as that above, September 11,

[5] Fifty cents in American money is the equivalent of .835906 grams of gold .900 fine.

1919, made United States gold legal tender in Salvador at the rate of two colones to the dollar. The plan was not to coin any national gold but to use United States gold as the basis of the new system. American bank notes, although not legal tender, were given free circulation and the banks in Salvador were required to receive them. A decree in December 1920 made them receivable for all government dues also. When the moratorium should be lifted the banks were to redeem their paper notes in American gold if national gold coins had not yet been minted.

Another monetary law was adopted in July 1920 which provided in more detail for the new system, and also arranged for the subsidiary money. This law declared that no foreign money was legal tender in Salvador, with the exception of American gold and silver coin, which should enjoy legal tender until national money was coined in sufficient quantity. Thus United States silver money has a greater legal tender quality in Salvador than in the United States, since in the United States subsidiary silver money is legal tender only in limited amounts, while in Salvador the law contains no limitations.

The new laws declared the exportation of silver money to be free, provided the exporter first guarantee to bring the proceeds of the sale of the silver back into Salvador in the form of American gold.

The importation of American money and the exportation of silver money by the banks and by private individuals began as soon as the monetary law of September 1919 was enacted. Over eight million dollars in American gold was imported into Salvador, most of which was imported within six months after the law went into effect. The exportation of the old silver money, according to official records, totalled about six and one-half million pesos. This exportation was also nearly all accomplished within six months

after the passage of the law, and at a time when the price of silver was practically at its maximum. A more auspicious time for the selling of the old silver could not have been found.

The substitution of gold for silver was rapidly pushed forward by the banks, and in January 1920 a sufficient amount of gold was on hand so that the moratorium was lifted and the banks began redeeming their notes in gold on demand at the rate of two colones to the dollar. This marks the beginning of the gold standard in Salvador. The period of paper money thus came to an end six months before the date fixed by the moratorium law of 1914. The law said the moratorium should continue until one year after the signing of peace in Europe, which would have been in June 1920. However conditions were such that on January 8, 1920 the three banks formally declared their readiness to resume specie payments, now in American gold. The Minister of Finance accepted their proposal and on January 15, 1920, full resumption was inaugurated, bringing with it the gold standard. American gold immediately began circulating freely from hand to hand.

During the last six months of 1919 exchange rates on New York declined so that dollars were at a discount, on the basis of two colones to the dollar. The cause of this fall in the value of the dollar is not far to seek. In the first place there had been a profitable coffee crop so that the supply of foreign drafts increased. In addition to this, Salvador was exporting large quantities of silver money and selling it in foreign markets. Part of the proceeds from the sale of the silver was used to purchase American gold for importation into Salvador, but the balance was thrown on the exchange market and as funds accumulated in New York dollar drafts became plentiful and cheaper. The fact that gold was being imported in large amounts served to limit the discount to which drafts might otherwise have gone. Rather than accept too great

a discount in selling a draft, a person could afford to bear the expense of importing gold which was now legal tender in Salvador. The following table shows the course of exchange rates in Salvador on New York.

RATES FOR SIGHT DRAFTS ON NEW YORK
Colones for 100 dollars
Figures furnished by Banco Occidental

	1919		1920		1921		1922		1923	
	HIGH	LOW	HIGH	LOW	HIGH	LOW	HIGH	LOW	HIGH	LOW
January	C212	205	C196	185	C216	208	C202	199	C202	199
February	212	200	200	193	214	207.5	203	198.5	201	199
March	215	200	200	196	215	208	203	199.5	202	200
April	215	201.5	207	199	225	212	204	199.75	205	200
May	212	206	205	200	213	209.5	206	202	207	204
June	209	195	203	200	213	209.5	204	202	206	202.5
July	198	190	211	202	218	211.5	205	202.5	207	202.75
August	194	187	208	204	218	206.5	210	205	207	205
September	195	190	208	204	208	201.25	208	205.5	206.5	202.5
October	195	192	218	210	205	202.25	208	201	203	200.75
November	193	183	226	208	213	203	205	200	203	201
December	195	189	215	208	205	199	203	200.5	202.5	201

	HIGH	LOW		HIGH	LOW		HIGH	LOW
1911	258	244	1916	293	289	1921	225	199
1912	255	229	1917	275	252	1922	210	198.5
1913	255	231	1918	264	210	1923	207	199
1914	350	228	1919	215	183			
1915	311	229	1920	226	185			

It will be noticed from the above table that the year 1919 was an especially appropriate time for the inauguration of currency reform on the basis of two colones to the dollar. During the years preceding 1919 the peso was not worth as much as two to the dollar according to exchange rates. In fact for much of the time three to the dollar would have been closer to the market value, and not since about 1905 did the peso approximate a value of as

much as two to the dollar. In February 1919 two paper pesos would buy one dollar and in June and the months following they would even buy more than one dollar. Thus the fifty cent unit adopted by Salvador, although a little high in value on the basis of exchange rates for previous years, was close to the market gold value of the peso at the time it was adopted. At the time the rate was selected gold was depreciated throughout the world, so that the purchasing power of the new unit was probably not far from that of the old peso.

However, the general depression and deflation beginning in the latter part of 1920 which affected nearly all the countries of the world, raised the purchasing power of gold, and Salvador at the present time doubtless has a unit of somewhat greater value than the old peso, more like the peso of a few decades ago. Index numbers of prices in Salvador are not available and it would be difficult to make an accurate comparison of the values of the peso and the colón.

The fifty cent unit is a fortunate unit for purposes of trade with the United States and with countries where the dollar predominates. Its size is well adapted to the needs of the people of Salvador. Nicaragua, Honduras and Salvador now each have units easily convertible into American dollars, and more or less based on the American dollar. The Mexican peso with a value of $.4985 is very close in value to the colón of Salvador.

Chapter VIII

SALVADOR ON THE GOLD STANDARD

1. *Business depression and foreign trade*

THE gold standard had functioned only a few months in Salvador when the depression of 1920 and 1921 seized the countries of the world, converting many profits into losses. The depression was felt especially severely in Salvador due to the way the prosperity of the country is dependent almost entirely upon the coffee industry. The price of coffee fell very rapidly in 1920, causing great losses to the coffee growers and exporters.

Salvador is an important coffee producing country and ranks next to Guatemala among the Central American states as regards the quantity of coffee shipped. The coffee plantations of Salvador are owned almost entirely by natives, although recently the number of foreign owners has increased. Salvador is the only one of the Central American countries which does not grow bananas commercially, and thus is especially dependent upon the coffee industry in her foreign trade. Salvador is not able to grow bananas profitably because her territory does not extend to the Caribbean seaboard where bananas grow so prolifically.[1] Since Salvador has no outlet on the Atlantic side of the isthmus her coffee shipments all proceed from Pacific ports, and go to San Francisco or go through the canal to European countries.

Before the war Salvador sent her coffee to the United States, France, Germany, Great Britain, Italy, and Austria. The war cut off shipments to Germany and Austria, and reduced those to other European belligerents very materially. The United States for

[1] Projects have recently been considered for growing bananas along the Pacific coast of Central America.

several years prior to the war had come to be the leading market for Salvador's coffee, and with European markets shut off, the United States received in 1917 more than half of the entire shipments. In 1918 the United States received about ninety per cent of the coffee exports. Increased amounts were sent during the war to Norway, Holland and Switzerland. Since the war large shipments to Europe have been resumed, although the United States has a stronger position than ever as the leading market for Salvador's coffee. Some of the coffee sent to the United States is re-exported to the Orient and Canada.

The situation in regard to imports was very similar to that described above as regards coffee exports. Imports into Salvador came largely from the United States and Great Britain, followed by Germany, France, Italy and Belgium. The war made trade with the European countries difficult so that Salvador was forced to buy most of her goods in the United States. American manufacturers not familiar with export trading shipped goods to Salvador, and merchants in Salvador in many instances were not satisfied with American goods or the terms of credit granted. However, since the close of the war American goods have held the dominant position in Salvador, a position which they were beginning to attain prior to the war.

In addition to shipments of coffee, other articles of importance which enter into the export trade of Salvador are, precious metals, sugar, indigo, balsam, hides and rubber. The chief articles of importation are food products, drugs, textiles, shoes and other manufactured articles, especially iron and steel articles. Figures for the foreign trade of Salvador are as follows.

Exports and Imports of Salvador

Data taken from Official Reports

	IMPORTS	EXPORTS
1911	*C* 13,627,000	*C* 22,208,000

	IMPORTS	EXPORTS
1912	C16,937,000	C22,342,000
1913	15,246,000	22,528,000
1914	12,396,000	26,991,000
1915	10,055,000	26,409,000
1916	14,555,000	29,012,000
1917	17,173,000	26,751,000
1918	15,355,000	24,800,000
1919	20,918,000	24,584,000
1920	25,257,000	35,888,000
1921	16,793,000	16,959,000
1922	15,279,000	32,427,000

The period of boom and prosperity which immediately followed the close of the war brought good times to Salvador. The high prices for coffee yielded good profits to the growers and exporters. Also the silver situation, described above, brought increased wealth to the country. The people were prosperous and bought freely. Importing merchants sold large amounts of goods in spite of the high prices, and, anxious to realize more profits, placed large orders abroad, often at extravagantly high prices. Exporters in the United States and elsewhere were unable to keep up with the growing trade following the close of the war, and in making shipments frequently cut down the size of the orders received. This led some of the merchants in Salvador to order more than they really desired, expecting to have the order reduced by the manufacturer abroad. Conditions were extremely inflated and when the collapse came the country found itself in perhaps the severest depression ever experienced.

During the last half of 1920 coffee prices fell from their abnormally high peaks, and the large profits which had been anticipated were quickly wiped out and converted into losses. The 1920 coffee crop also was considerably under normal, a fact of no great concern until the price of coffee began to fall. Since the prosperity of the country depends so greatly upon the condition of the coffee

industry, a slump in the coffee market meant hard times for the people generally.

At the same time that the price of coffee fell, the prices of general merchandise also fell in the United States and elsewhere as the business cycle started on its downward swing. The merchants in Salvador found that they were overstocked with goods bought at prices much higher than the prevailing market prices, and which they were now unable to sell. The people of Salvador, with reduced incomes, had little money with which to buy, and were buying only goods which were necessary. Luxuries which had been bought freely a few months previously were no longer in demand.[2] Orders which importers had placed abroad and expected to have had only partially filled, were now filled in full and at the old high prices. Cancellations of orders as far as possible resulted, but the merchants found themselves stocked up with goods which they could not sell, bought at high prices and not yet paid for. They found great difficulty in meeting their foreign obligations, with dollars becoming more expensive.

Exchange rates for dollars began to rise early in 1920, making payments abroad more expensive for local merchants.[3] In November 1920 exchange rates reached the maximum, when 226 colones, gold or paper, were needed to purchase 100 dollars in New York. The rates had been at a discount during the last half of 1919, and then went to par after the banks began redeeming their notes in United States gold at two colones to the dollar in January 1920. The rates were at a discount when good coffee prices and profitable sales of the silver in the old silver money made funds in New York plentiful. They rose in 1920 as the sales of silver were completed

[2] The Government of Salvador finally placed an embargo upon the importation of luxuries.

[3] See table of exchange rates on p. 79.

and as the demand for drafts increased. The prosperity of the year before had led merchants to import an unusually large amount of goods, and they needed foreign drafts to pay for these goods.

The coffee situation also tended to push up the exchange rates. The 1920 crop was considerably smaller than normal, and it was seen that coffee exports would be relatively light, meaning that bills would be scarce. Combined with a small coffee crop, the price of coffee was falling precipitously in foreign markets, so that what coffee was exported would not bring the anticipated values.

Exchange rates went to the gold export point in the latter part of 1920, and the newly imported American gold began leaving the country. The exportation of gold was a logical result and remedy for high exchange rates, an ordinary event in gold standard countries. The exodus of the precious metal caused anxiety in Salvador, and the Minister of Finance issued an order to the customs officials not to allow the exportation of gold without a permit. A permit was difficult to obtain and this interference with exportation doubtless caused exchange rates to go several points higher than otherwise would have been the case. It hampered the workings of the normal forces which tend to restore equilibrium when the rates get out of adjustment.

American money flowed out of Salvador in large quantities, either by permit or clandestinely. Smuggling money out of the country was a relatively easy matter. American paper money was much easier to export than gold money, and since no permit was required for the exportation of paper money, American paper money was at a premium of about three per cent in terms of gold money. One hundred dollars in American paper money would purchase over the counter one hundred and three dollars in American Gold money. Official records in Salvador showed the

exportation of about one million and a half dollars in American gold coins, and the Minister of Finance estimated that more than this amount left without being entered in the records. In addition to this practically all the American paper money left the country.

The exportation of a large percentage of the American money might be taken as evidence that the arbitrary amount of gold imported for the introduction of the gold standard was an excessive amount in relation to the existing price level and trade demands, and that the exit of gold was part of the process of adjustment to an international price equilibrium. Or it might indicate that the colón was overvalued in terms of gold by the new law as compared to the old peso, and that with a unit of greater value fewer coins were needed. On the other hand the period was one of price readjustments throughout the world, and the commercial situation in 1919 when the gold standard was arranged for was almost the reverse of that existing in the winter of 1920-21. To have determined accurately the proper amount of gold needed to establish successfully the gold standard would have been a problem of some magnitude, and it was better to have had too much gold than too little.

The banks in Salvador were in a difficult position during the period of the depression. Their generous gold reserve of ten and one-half million colones at the first of 1920 was reduced to something over three million colones by the middle of 1921. They viewed this withdrawal of their gold with alarm, and talk of another moratorium was heard. Rumors that suspension of specie payments was about to be inaugurated frightened people, and in September 1920 a run on the banks for gold began. For several months following the banks were subjected to a heavy drain on their reserves. However, they were able to meet all the demands for gold, and specie payments were maintained. Bank notes were

brought to the banks for redemption so that the circulation declined from about fourteen and one-half million colones at the first of 1920, to about six million colones by the middle of 1921, an unusually large contraction.

The banks were heavily loaded down with non-liquid paper, and were forced to discontinue almost completely the extension of credits. Coffee growers, merchants and others who had borrowed from the banks were unable to meet their notes as they came due, which left the banks in an embarrassing position. Coffee growers are financed to a large extent through the local banks. In the spring or summer the grower comes to the bank for accommodation and gives his two name note, in conformity with the law, running usually for about nine months time. Later, as he needs more funds he gives shorter term notes which all mature together at the time the crop is harvested, which is about the end of the year. Inasmuch as the coffee growers were in need of money and could not get accommodations at the banks, the price of coffee fincas declined.

Since the banks were not extending credits even on the best of security, interest rates rose above their customary levels. Normally, interest rates are about one per cent a month, but during the stringency of funds those who had money to loan could obtain interest at the rate of as much as twenty or thirty per cent per annum. The banks were unable to grant further credits since doing so would cause additional demands for gold, and the reserves were already down to the limit.

Conditions in the coffee industry improved in 1921 and 1922, and as liquidation of indebtedness took place the country became more prosperous. Gold stopped pouring out of the country and confidence was restored. Exchange rates declined and by the latter part of 1921 the rates were close to par. Business conditions in general were very much improved. With the return of prosperity

the bank note circulation increased, and at the first of 1923 amounted to nearly nine and one-half million colones, an increase of more than fifty per cent over the low point of the middle of 1921. The gold reserves were also built up during this period, and at the first of 1923 amounted to over six million colones.

2. *Return to circulation of old silver money*

THE gold standard laws provided for fractional money to consist of fiduciary coins of silver and nickel. The minting of these coins was to be arranged in the United States. The law demonetized the old silver money both national and foreign, with the exception of the small coins of twenty centavos and under. At the time the law was passed in September 1919, it will be remembered, silver money was not in circulation due to the inconvertibility of the paper bank notes and the high price for silver. Thus the demonetization of the old silver money attracted but slight attention at the time of the act.

When the price of silver fell in the latter part of 1920, however, the silver in the old peso became worth less than 50 cents in United States money, the value given the new unit, the colón.[4] The coins were now worth more as money at the rate of fifty cents to the peso, or two to the American dollar, than as silver bullion. The silver coins which were still in existence, that is, those which had been hoarded and not exported or melted down, began reappearing in circulation where they had not been seen since early in the war when they were driven out by the irredeemable bank notes. The situation in Salvador was analogous to that existing in Honduras where the peso had been made the equivalent of fifty cents in

[4] When the market price of silver is seventy cents an ounce the silver in the peso of 25 grams .900 fine is worth approximately fifty cents. The price of silver fell to seventy cents an ounce in November 1920 and continued falling until it reached nearly fifty cents in 1921.

American money, and where the fall in the price of silver also brought the old silver money back into circulation.

Honduras and Salvador were the only Central American countries prior to the war where the silver standard and the miscellaneous collection of old silver coins still prevailed. It was thought in 1919 that all this old silver money was drawn out of the country by the high prices obtaining abroad for silver, and would never return to cause trouble. However, a surprisingly large amount did not leave the country but went into hoards or was held by speculators waiting for still higher prices. Many of the people of Central America are suspicious of banking institutions and prefer to keep their savings stored away in the form of coin. Thus when the price of silver fell, gold was thought to be a better metal to hoard than silver. Rumors as to the doubtful value of silver money caused it to come pouring into circulation.

The Minister of Finance in Salvador issued an announcement in February 1921 advising the people that the silver money had been demonetized and was no longer receivable by the Government, also urging the people not to accept it. The statement contained an error in that only the larger denominations of the silver coins has been demonetized by the gold standard law, while the Minister declared that all the silver coins were no longer legal tender.

The people who had their small savings stored away in silver money saw in the demonetization announcement a loss in their savings and strongly resented what they thought was an attempt on the part of the Minister of Finance to deprive their money of its value. Suspicions were passed about as to the motives behind the announcement, and with official corruption a commonplace in Central America, it was rumored that large personal gains were resulting somewhere.

A popular protest was raised against the demonetization, and complicated by political difficulties violence broke out. The Minister of Finance was forced to flee to Guatemala. The people of the market place, especially the women, were leaders in the disturbance which caused chaos in the capital for a few days, so that the Government came close to falling. The Government under pressure hurriedly decreed that until the new fractional money should arrive in Salvador the old silver money should circulate freely.

The following week when the trouble had subsided the National Assembly decreed that the money which had been made legal tender a few days previously, until the fractional money arrived, was only the Salvadoran money and United States money. The other foreign silver was no longer legal tender. This law also prohibited the importation of silver money with the exception of United States silver money.

As time went on it developed that only a relatively small quantity of the old silver money was still in Salvador, and that it constituted a small portion of the total circulation. The new fractional money soon began arriving in Salvador, and the monetary situation under the gold standard was completely satisfactory. Salvador is now firmly on the gold standard and enjoys relatively stable exchange rates with gold standard countries, which is a great advantage in facilitating trade with these countries.

Chapter IX

HONDURAS ON THE SILVER STANDARD

1. *Monetary history prior to* 1915

WHEN Honduras was under Spanish rule the monetary system was that of Spain. In addition to the regular Spanish coins, there were other foreign coins and a certain amount of "macacas," pieces of silver cut to odd shapes and bearing the official stamp. About 1650 when an increased amount of silver had been taken from the mines, small pieces of silver cut from silver sheets began to appear; they were similar to the "macacas" but lacked the Government stamp and were not locked upon as official currency. However, they were acceptable to the workers and circulated freely. The Spanish authorities saw the unsatisfactory character of such currency and endeavored to replace it with other currency, but were unsuccessful, and a large part of the money in circulation during this early period was "macacas" and small pieces of unstamped silver.

In 1733 the King of Spain established a mint in Guatemala. Tegucigalpa ordered coins from this mint, and put a large number of them into circulation so that the currency came to be of a more regular character. The small pieces of silver disappeared but the "macacas," or "moneda cortada" as they were called, continued to form an important part of the currency; in fact they continued to circulate until about the middle of the nineteenth century. In some of the outlying sections they did not disappear until a few years ago.

Honduras obtained independence from Spain in 1821. In 1822 a die for coining money was brought to Tegucigalpa from Mexico and reales and half reales were coined in "moneda cortada." There

appears to have been considerable dishonesty in connection with the work, which was performed in a convent, and the coinings were soon abandoned. Honduras then had some coins struck in Costa Rica where by this time a mint had been established. A few years later Honduras again commenced the coinage of money in the "Caja Real" as its mint was then called.

The fineness of the coins was reduced in 1832 to .500 so that the coins were fifty per cent copper and fifty per cent silver. These were called popularly "moneda de media leche," "media leche" meaning milk that is half water. From this time on the debasement continued until by 1848 the coins contained only a very small amount of silver, and by 1857 and 1858 they were almost pure copper. Some money was composed of a mixture of copper and zinc, and even some iron money was put out. These debased coins drove the silver from circulation, and it did not return again in large amounts until in the seventies.

Coinings ceased in 1858 when the mint was closed and served as a barracks for soldiers, and were not resumed until 1879. Shortly after 1860 some copper money was introduced from England by private individuals who had it coined according to contract with the Honduran Government. This money, called "moneda provisional," at first circulated freely, but as its quantity was increased it became depreciated and finally ceased to circulate altogether. A similar experience was undergone in 1869 when the Government put into circulation nickel money that it had ordered coined in France. At first the coins circulated at their face value, but as the Government put out large amounts they became greatly depreciated until ultimately they were rejected completely as money.

After the disappearance of the nickel money, silver again began to come into circulation. The silver was a miscellaneous mixture of foreign money, money from Chile, Peru, Mexico and other

Spanish countries. The coins were not identical as to weight and fineness, but in general circulation there was little discrimination between the coins. The larger denominations appear to have been brought into the country before the smaller denominations, and there was a consequent lack of small change. The Government put into circulation again some of the copper "moneda provisional" of the early sixties which facilitated the small transactions.

In 1879 a monetary law was adopted which aimed to introduce more uniformity into the currency system.[1] The law provided that the unit be the silver peso of 100 centavos consisting of 25 grams of silver .900 fine. It also provided for silver coins of 50 and 25 centavos of proportional weight to the peso and of similar fineness, also for fiduciary silver coins of 10 and 5 centavos and for copper pieces of 1 and ½ centavos.[2]

The law referred briefly to gold money and provided that it might be coined later if circumstances permitted, at a weight to be fixed by the executive. The coinage of gold money was begun in 1888 and the gold peso was worth, according to its metallic content, a little less than the American dollar. The gold coins struck were of the denominations of one, ten and twenty pesos. Only a small amount of gold money, however, was actually minted, and since the price of silver was falling at this time, gold money never stayed long in circulation. The law of 1879 also provided for the re-establishment of the mint which had not been in operation for over two decades.

Upon this law of 1879 was based the recent monetary system of Honduras. However, Honduras has never enjoyed a circulation consisting entirely, or even principally of its own coins. At the

[1] cf. Honduras, *Leyes de Hacienda*, 1866-1903, Decreto 46, pp. 134-145.

[2] In 1899 the fineness of the 25 centavo coins was reduced from .900 to .835, thus making these fiduciary coins. cf. op. cit., Decreto 125, pp. 950-951.

time of the law of 1879 the bulk of the circulation consisted of coins from various Central and South American countries. Certain sections of the country still retained the silver coins of irregular shape, the "macacas" or "moneda cortada," dating back to the early Spanish days.

Coinings by the mint in Tegucigalpa in accord with the new law were considerable but did not suffice for the needs of trade nor to displace completely the foreign coins. Furthermore, the Honduran silver coins contained such a large proportion of gold, which had not been separated from the silver, that most of them were promptly withdrawn from circulation and exported for the extraction of the gold. The circulation of foreign money in Honduras was recognized officially in 1894 when money of Nicaragua and of El Salvador was made legal tender. The law declared that Peruvian money might be received at the option of the public. It is evident that this declaration did not alter the status of Peruvian money other than to give its circulation a semblance of official sanction. Although the law recognized no other moneys, considerable amounts of the coins of other Latin-American countries were imported, especially those of Guatemala and Chile. Most of the fractional coins imported were .835 fine or less, and as a result the pesos were exported in preference to the cheaper moneys which remained in circulation, an example of the operation of Gresham's law.

To remedy the situation a law was passed in 1909 which placed a tax of 25 per cent upon the importation of foreign silver coin of a weight and fineness less than the peso, and prohibited altogether the introduction of coins of a fineness less than .835. This measure was directed especially against the Nicaraguan coins, debased by Zelaya, which are said to have been imported in considerable amounts by the German houses. The law also placed a

tax of 15 per cent upon the exportation of coins of weight and fineness similar to the peso. The lower grade coins that had come into the country were absorbed into the circulation and passed at par with the other coins; an interesting refutation of the bullionist theory, coins of less bullion value circulating at par with coins of greater bullion value, although nowhere were they redeemable in the latter. The banks made no distinction between the different classes of silver except for purposes of export, where coins of the greatest weight and fineness were selected.

Honduras was on the silver standard and when the price of silver fell during the last quarter of the century the country experienced a great rise in exchange rates on gold standard countries, accompanied by difficulties to foreign trade. From 1894 until 1915 the price of silver was more or less stable, and fluctuations in exchange rates were not as great as during the preceding period.[3]

2. *The silver standard and exchange rates*

In the latter part of 1915, the price of silver began its upward movement, and silver money was exported in such quantities that business began to be embarrassed for lack of sufficient currency. The law of 1909 was strengthened by a new law in January 1916, which provided that the export tax of 15 per cent be applied also on the exportation of silver bullion proceeding from the melting down of silver money. Since Honduras is an important silver-producing country, such a law was difficult of enforcement and much money found its way out of the country. Furthermore, the price of silver continued to rise until quotations in New York for pesos were sufficiently high to make profitable their exportation, paying the 15 per cent tax. The scarcity of currency became so acute that in April of the same year, 1916, the exportation of silver money in whatever form was prohibited. Since vigilance and con-

[3] cf. chart on p. 97.

trol over the ports and borders was imperfect, the law proved ineffective to prevent such profitable transactions, and clandestine exportation continued. Certain of the government officials were alleged to have been participants in the illegal traffic.

The following chart shows the course of the value of the silver in the Honduran peso during the last forty years, expressed in terms of American money. The upper and lower lines of the shaded section represent the high and low price, respectively, of each year.

Since in gold standard countries the Honduran peso is worth only the silver it contains, when the price of silver in foreign markets rose, beginning in 1915, the purchasing power of the peso abroad likewise rose. The increased gold value of the peso was expressed in the foreign exchange rates on New York at Tegucigalpa, which are shown in the chart on page 98.

It will be noted that until the rate was stabilized in 1918, this curve resembles closely the corresponding section of the former chart representing the value of silver in the peso. There was a rise in 1912 and 1913 followed by a fall in 1914 and 1915. In the latter part of 1915 the price of silver began its upward movement.

The chief sources of drafts at Tegucigalpa are the New York and Honduras Rosario Mining Company which sells drafts against silver that it has exported in order to secure money for its local running expenses, and the fruit companies which sell drafts for similar purposes. The demand for drafts is chiefly from the merchants who import miscellaneous articles of merchandise. The seasonal fluctuations in the demand and supply of drafts is not very pronounced; the chief cause of variation is a reduction in the exportation of bananas during the months from November to April. Fluctuations in exchange rates, other than those caused by variations in the price of silver, are due to temporary market conditions.

CHART III

Value of the Silver in the Honduran Peso, 1880-1923

High and low, in terms of American money; cents per peso.

[*Peso contains 25 grams of silver .900 fine*]

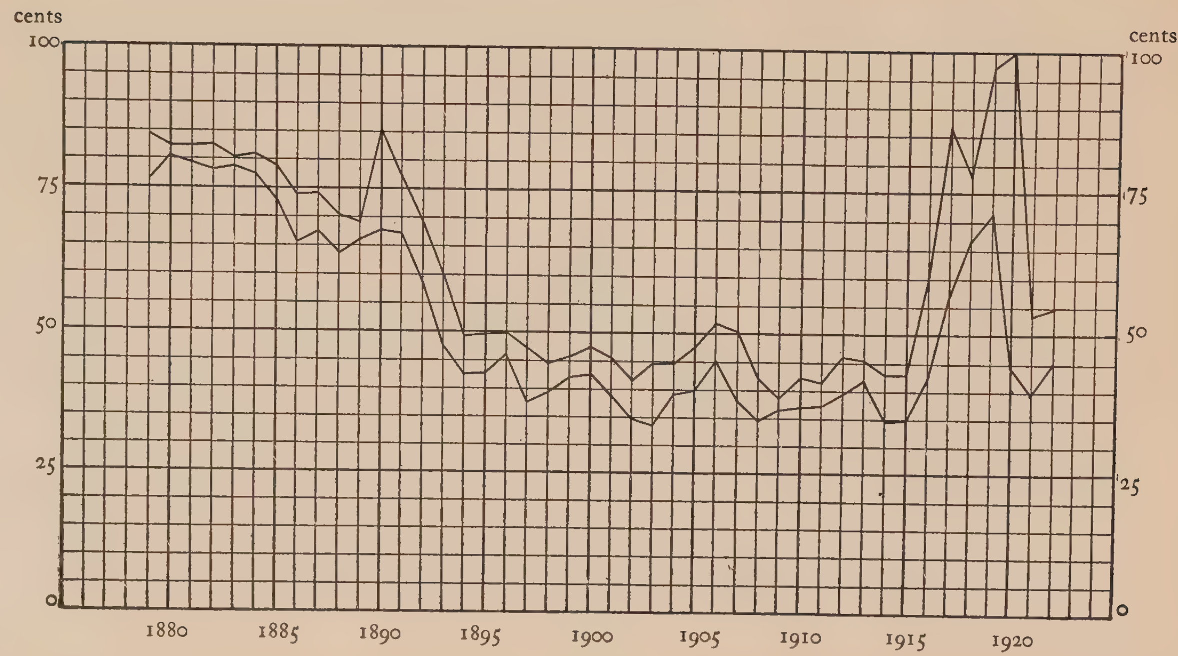
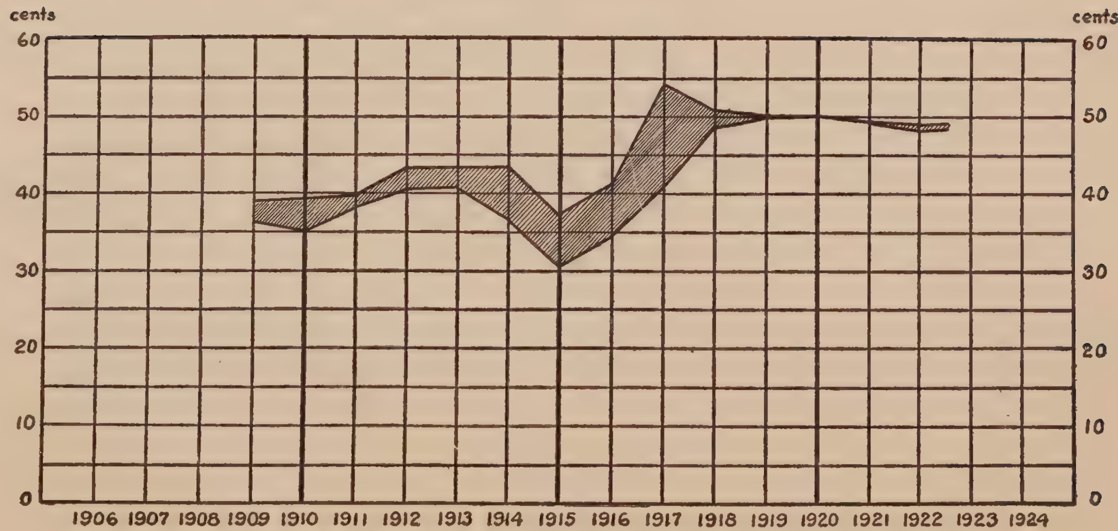


CHART IV

EXCHANGE RATES ON NEW YORK: VALUE IN AMERICAN CURRENCY OF ONE PESO[4]



[4] Figures for the years 1912-1920 supplied by the New York and Honduras Rosario Mining Company; figures for the years 1909-1911 supplied by the Banco de Honduras. The curves which show the high and low rates for each year do not represent the maximum and minimum rates of that year but represent the high and low of the monthly averages, which gives a more accurate picture of the general movement of the rates.

3. *Foreign trade and the price of silver*

As the price of silver rose and exchange rates fell, importing merchants paid less when buying their goods, and the sale of these goods in Honduras at prevailing prices yielded them greater profit. The increase in the purchasing power of the country's money, stimulating imports, caused an increased quantity of commodities to enter the country. At the same time other factors tending to increase imports were present, especially the development of new enterprises on the North Coast by the fruit companies and the stocking up with goods after the war. The increase in importations can be seen from the following official statistics, which, it should be added, are not entirely reliable, especially in respect to exports from Honduras.

EXPORTS AND IMPORTS OF HONDURAS, 1910-1922
In terms of United States gold; 000 omitted

YEAR	IMPORTS	EXPORTS	EXCESS OF IMPORTS
1910-11	$ 3,561	$2,908	$ 653
1911-12	4,317	3,080	1,237
1912-13	5,133	3,181	1,952
1913-14	6,625	3,421	3,204
1914-15	5,875	3,458	2,417
1915-16	4,542	4,191	261
1916-17	6,293	5,353	940
1917-18	4,784	4,587	197
1918-19	6,931	5,998	933
1919-20	12,861	6,945	5,916
1920-21	16,723	5,429	11,294
1921-22	12,804	5,386	7,418
1922-23	14,342	10,016	4,322

The figures for imports are more exact than those for exports since certain clandestine exportations occur which do not enter into the above figures. Furthermore, in compiling the statistics the practice exists of fixing arbitrarily the prices of the articles ex-

ported, giving them in general a price lower than their market value.

Since more than 90 per cent of the total exports of Honduras goes to the United States, it is interesting to compare the statistics of the two countries. During the twelve months ending July 31, 1920, Honduras exported to the United States $6,665,675 according to Honduran statistics. During the twelve months ending June 30, 1920, the United States imported from Honduras according to American statistics $8,290,122 without counting gold and silver which are not included in the American figures of general commerce and which amounted to about $2,000,000. From these data it is possible to estimate that the exports of Honduras to all countries during the year 1919-20 were approximately $10,500,000, or fifty per cent more than the figures noted by the Honduran fiscal offices. Regarding importations into Honduras, both American and Honduran figures are in substantial harmony.[5]

The stimulus to importation of goods due to a rise in the price of silver normally continues only so long as a variance exists between prices at home and prices abroad expressed in the same silver unit. As coin leaves the country the currency is contracted and prices tend to fall. Increased merchandise imports hasten the process by providing a greater supply of goods. This together with the smaller supply of money tends to result in a lower level of prices, other things remaining equal. When prices are such that the silver peso will purchase relatively as much at home as abroad it no longer is profitable to export silver.

However, a reduction in the price level takes considerable time to work itself out, and the part played by custom, habit, and other psychological factors in the determination of prices is not to be

[5] cf. Honduras; *Memoria de Hacienda y Crédito Público*, 1919-20, pp. 15-16.

underestimated. When the price of silver began to rise merchants in Honduras were stocked up with goods, and business was adjusted on the basis of the accustomed level of prices. The advance in the price of silver was so great and occurred so rapidly that the immediate results when through exports and hoarding Honduras was denuded of the major portion of her silver, were disturbances to business and banking. People became nervous and there was an excited rush to the banks for money. As the banks demonstrated their ability to meet the demands in silver the trouble subsided and confidence was restored. A shortage of currency with the resulting inconveniences was the most pronounced effect that the country experienced. Had the rise in the price of silver been gradual and spread over a period of time, Honduras would doubtless have retained a considerable portion of her silver in circulation and have experienced a fall in the level of prices, due to the loss of a large part of her currency to foreign countries where the demand for silver had become intense, and had necessitated a readjustment between the amounts of silver in the arts and in monetary channels.

If banking and credit in Honduras had been highly developed, the monetary crisis would have been more intense. The two banks in active operation, the Banco de Honduras and the Banco Atlántida, have notes in circulation which are backed by a legal reserve of forty per cent and fifty per cent, respectively. As the price of silver advanced, their notes were rapidly presented for redemption and the outstanding circulation of the two banks contracted, as may be seen from the table on the next page.

Bank Notes in Circulation in Honduras

	BANCO ATLÁNTIDA	BANCO DE HONDURAS
June 30, 1918	*Pesos* 291,909	*Pesos* 202,846
December 31, 1918	139,699	160,484
June 30, 1919	79,140	112,239
December 31, 1919	83,165	69,106
June 30, 1920	179,012	41,449
December 31, 1920	386,710	34,357
June 30, 1921	217,097	
December 31, 1921	210,992	
June 30, 1922	175,350	
December 31, 1922	155,223	
June 30, 1923	170,240	

Chapter X

HONDURAS ON THE GOLD STANDARD

1. *Banco Atlántida permitted to redeem its money in American money*

ON the North Coast of Honduras, which is dominated by American companies in the banana trade, a certain amount of American money has been in circulation for several years. But little of this money ever found its way to the interior. The northern part of the country under the influence of American capital and with fast and frequent steamship service to New Orleans has different economic interests from the other sections of the country where the method of living has not changed greatly since the days of Spanish rule. The capital is only about 200 miles from the North Coast ports, yet the journey, which is over difficult country, consumes nearly a week on the average and must be made partly by pack train, although a road is now under construction. The North Coast with some American currency in circulation was not affected by the exodus of silver to the same degree as the interior sections of the country.

Various remedies for alleviating the monetary situation were suggested. Inasmuch as a certain amount of American money already was circulating in the country the Banco Atlántida, controlled by American capital and with its main office on the North Coast, proposed that this circulation be increased, and extended to the entire country. Accordingly a contract was negotiated on March 21, 1918, between the bank and the Government which was then in need of financial assistance, the terms of which provided that, in addition to granting further credits to the Government, the bank "will exchange. . . its notes at option of bearer in current silver

money, American money or in bank drafts at 2 to 1 as long as quotations of soles in New York do not go below 53 cents."[1] The contract is ambiguous and was evidently of no benefit to the bank. The bearer of the bank's notes was given the option of declaring in what class of money he wished the notes redeemed. He would not select to have his paper peso redeemed in 50 cents of United States money when he might receive for it a silver sol[2] which was then being quoted in New York at 75 or 80 cents. The contract did not give the bank relief in meeting the demands for redemption of its notes in silver soles, which were scarce and difficult and expensive to procure. The proviso "as long as quotations of soles in New York do not go below 53 cents" protected the bank, in the event of a fall in the price of silver, against loss from being required to redeem its notes in American money. It was estimated that if soles were quoted at less than 53 cents (which means that the price of silver is between 73 and 74 cents per ounce) the exportation of soles—worth 50 cents in Honduras—would no longer be profitable, and if the quotation went much below 50 cents the danger would exist of soles being sent to Honduras for redemption in American money at 50 cents to the sol. This protection to the bank was a protection against a danger which was created by the contract, a contract which apparently was of no value to the bank, nor to the public who had no desire for American money.

The bank, however, soon realized that the contract was unsatisfactory, and took up the matter with the Government. The President of Honduras was in need of funds from the bank and was told that to obtain them it would be necessary to strike from the above contract the phrase "at option of bearer" and substitute

[1] This contract has never been published.

[2] The word *sol*, the name of a Peruvian coin, is used synonymously with the word *peso*.

for it "at option of the bank." The President was hesitant, but needing 60,000 pesos urgently that morning, said he would strike out "at option of bearer" and leave the question open. The phrase in question being removed, the bank holds that by implication the option as to redemption rests with the bank. "The bank" is the subject of the sentence which reads "the bank. . . will exchange its notes in current silver money, American money or in bank drafts at 2 to 1 as long as quotations of soles in New York do not go below 53 cents." This change in the contract was accomplished on May 1, 1918, and gave the bank relief from the obligation to meet its notes in a class of money which was rapidly being withdrawn from business channels, and was the first step toward the adoption of American money.

The contract of March, 1918 (revised in May), provided further, among other things, that the Government would receive notes of the bank in payment of fifty per cent of fiscal payments, then payable in silver money, the other fifty per cent to be payable in silver or in American money at the rate of two pesos to the dollar.

On September 13, 1919, a decree was issued by which a further step toward the definite adoption of the gold standard was taken. The bank was to guarantee its notes in American money in the same proportion established in its concession, i.e., with a reserve of fifty per cent. The decree furthermore relieved the bank of the obligation of redeeming its notes for a period of six months, during which period it would be able to import a sufficient amount of American money.

When this decree was issued the revolution, which resulted in the overthrow of the Government, was at its height. President Bertrand had fled from the country leaving his ministers in charge, who were in urgent need of funds and insisting that the bank grant them a loan. Reluctantly the bank consented to do this, securing

in return a six months moratorium on the redemption of its notes. The ministers, desiring funds, were prepared to assent to almost any arrangements. The bank then began putting out its notes freely, and as they came back, paid out United States fractional coin which it was importing and for which a considerable need existed. The decree was probably contrary to law, since the Executive's legislative powers are limited, but with conditions disturbed, before it could be so declared the bank was given an opportunity to change from a silver to a gold basis. Being on a gold basis, the bank concluded an arrangement in the same month, September 1919, whereby it was permitted to export 365,000 silver soles, paying the Government for the privilege of export, which was forbidden by law, approximately $30,000. This silver was sold at a time when the price of silver was nearly at its maximum. The bank also agreed to import $250,000 in United States fractional silver, and actually imported between $250,000 and $300,000.[3]

By an *acuerdo* of May 10, 1920, the bank was authorized to countermark its notes with the inscription "Redeemable at 200 per cent for American money of paper or metal." The bank holds that the acceptance of such notes constitutes a private contract and silences opposition which held that the decree permitting the bank to redeem its note in United States money was illegal since the bank's concession declared the notes redeemable in silver pesos.

The bank at the present time is firmly on the gold basis and since January 1920 has transacted its business in terms of United States money, although it receives silver for deposit and does a certain amount of business in terms of silver, keeping the accounts separate and paying as deposited.

[3] The New York and Honduras Rosario Mining Company also was permitted to export approximately 225,000 soles under a similar arrangement, and agreed to import $145,000 gold in United States fractional currency.

While the Banco Atlántida was introducing the country to American money, which as seen above was exceedingly advantageous to the bank as well as to the country at large, the Banco de Honduras, owned and controlled by native capital, was meeting its obligations in silver. As American money came into circulation and was adopted by the country at the rate of two local pesos to one dollar, the bank received and paid out the new money, but it still transacts the bulk of its business in terms of silver pesos, and has remained on the silver basis.

The notes in circulation of the Banco de Honduras have been reduced to a nominal sum as shown in the above table.[4] Since its notes are redeemable in silver it does not desire to have a large amount outstanding in the event of a rise in the price of silver.

2. *American money made legal tender*

To further stabilize the rate at which American money was exchanged for native money, an executive decree was issued on August 8, 1918, making American money legal tender at the rate of two pesos to the dollar. Although the decree made no mention of the gold standard which was foreign to the thoughts of the President and minister, it was a *de facto* adoption of the gold standard, declaring in essence that the monetary unit, the peso, might be treated as equivalent to 11.61 grains of fine gold, i.e., one half of the American dollar, in all transactions public and private. Debts being liquidated in the cheapest money possible, the peso would never be valued at an amount greater than the equivalent of 11.61 grains of fine gold. Whether it ever could be valued at less than this amount would depend upon the price of soles. Soles remaining legal tender, a sufficient drop in their price might bring them back into circulation and put the country once

[4] cf. p. 102.

more upon the silver standard. The experience of the country with this contingency when the price of silver fell in the latter part of 1920 and the first part of 1921, is discussed below.

The following is a translation of the decree of August 1918 which made American money legal tender.[5]

> "Considering that the clandestine exportation of silver money has created difficulties in exchange, and that American money has entered into circulation and is received in the fiscal offices at the rate of 200%, and that it is advisable to sustain this relationship; therefore the Cabinet of Ministers decrees—
>
> Article 1. American money and bank notes shall be legal tender, computing the rate of exchange at 200%.
>
> Article 2. The present decree will take effect from today and will be submitted to the National Congress for its approval.
>
> Tegucigalpa, August 8, 1918."

The Executive undoubtedly exceeded his legal powers in issuing this decree, seeking justification in the exigencies of the situation. But since the decree was approved by Congress, January 23, 1919, it obtained the full force of law.

The rate of two pesos to the dollar was approximately the rate of exchange prevailing at the time of the decree, as will be seen from the following figures:

Average Rates of Exchange at which the New York and Honduras Rosario Mining Company sold its Gold Demand Drafts to Merchants in Tegucigalpa, United States Cents for one Peso

1912	40.9	1915	33.7	1918	49.8
1913	42.2	1916	38.6	1919	50.0
1914	41.0	1917	45.6	1920	50.0

At the time of the decree, while the peso would purchase ap-

[5] Decreto 59, *La Gaceta;* August 12, 1918.

proximately fifty cents in a draft on New York, the silver it contained was valued at between seventy-five and eighty cents according to current prices. The exportation of silver money being prohibited, exchange rates and the price of silver did not move together, as noted above.

The people of Honduras needed to be educated to the use of American money. The silver in the peso was valued in foreign markets at more than fifty cents in American money, the legally established rate for exchange in Honduras, and the people had a feeling that they were being robbed of a part of the value of their money. For this, and other reasons, "grimbaks," as all American paper money was called, were at first in disrepute. The Banco Atlántida had a difficult task in putting American money into circulation and in urging the people and merchants to accept it and transact their business in its terms. Those having debts due them in pesos were not disposed to receive American money at a rate less than that existing in the foreign market. For a time American money passed at a discount in terms of the native money, which was encouraged by the Germans during the war, but as the native coin disappeared from circulation American money had the field alone.

Disputes regarding contracts that declared themselves payable in silver were brought into the courts. The courts decided that when a contract specifically stated that it was payable in silver it should be so paid, or if silver was not available it might be paid in American money of equivalent value at the current quotation for soles. On the other hand it was decided that when a contract stated "pesos" without specifying silver, American money at the legal rate of 200 per cent was lawful tender. A case was brought to the courts regarding a contract that declared itself to be payable in gold, and where the creditor, who was offered American paper money, refused the tender on the ground that the money

was not gold and that to convert it required additional expense. The court upheld the defendant and ruled that American money which was redeemable in gold, was to be considered the same as gold. The correctness of this decision has been questioned, though its expediency was generally admitted since American money is referred to commonly as "oro" (gold).

Chapter XI

RETURN TO CIRCULATION OF SILVER MONEY

1. *Fall in price of silver and reappearance of silver coins*

WHEN the price of silver declined spectacularly in the latter part of 1920, silver coins began to reappear in circulation. In November the silver in the peso, or sol, came to be valued at somewhat less than fifty cents, and the coins were now worth more as money at the rate of two soles to the dollar than as silver. When the market price of silver is seventy cents an ounce the silver in the sol is worth approximately fifty cents. The silver coins which had been hoarded and not melted down reappeared in circulation almost over night. Enjoying a fiduciary circulation in Honduras, many were imported from neighboring countries where they had been demonetized, or no longer passed currently. In Honduras they now began circulating in large numbers at the lawful rate of two pesos to the dollar.

A considerable sum in silver money proved to be still in existence. A large majority of the people either do not have access to the facilities offered by the banks or do not use them, and keep their small savings stored away in strong boxes. When the price of silver rose silver was thought to be a better metal to hoard than gold. Furthermore large quantities of silver were hoarded for speculative purposes, and while waiting for still higher prices, many owners failed to dispose of their holdings until the opportunity for profit had passed.

Estimates as to the quantity of the old silver coins still in existence have varied greatly as there is little upon which to base an estimate. The amount circulating in Honduras before the rise in the price of silver may be placed at between five and seven million

pesos, while that at present is probably not far from one and a half to two million pesos. The fear was entertained that they would continue to appear in such quantities that the country would be forced back to the silver standard. They would tend to drive out the American money, thus leaving the country with cheaper coins.

In January 1921 a law was presented to Congress demonetizing the old silver coins and prohibiting their importation. This would have been the final step in the abandonment of the silver standard and would have assured to the country the permanence of the gold standard. Only a limited quantity of the old coins were in actual circulation but many individuals had large sums of silver stored away and a vigorous popular protest was raised against the measure. It was charged that high government officials and the banks were to reap a profit from it. The measure met with favor in the northern part of the country where it was welcomed as a necessary piece of legislation, and where it was realized that the country was threatened with a return to the silver standard, and that Honduras was being made an asylum for homeless coins. In the southern and interior towns the fact that the measure was to prevent a return to the silver standard was in general no argument in its favor, but rather an argument against it.

After the introduction of the bill into Congress, the Minister of Finance issued a circular ordering the Custom Houses not to receive anything but American money, or bank notes redeemable in gold, a circular that was clearly beyond his powers. The excitement that resulted almost threatened the stability of the Government, and to calm the people the Minister of Gobernación issued a circular a few days later ordering the money accepted at par in all payments in accordance with the law of "2 for 1."

The introduction of the bill into Congress brought the silver coins into disfavor and caused them suddenly to go to a discount,

which at its maximum amounted to approximately twenty per cent. With much sentiment opposing the project, and many even favoring a return to the silver standard, the Government permitted the measure to die in spite of its warm reception on the North Coast. When the Government was seen to be weakening on the measure, and on a substitute measure which had been introduced and which went no further than to prohibit the importation of the coins and permit free exportation, the depreciation which the coins had suffered became less, and practically disappeared in Tegucigalpa and the southern part of the country. But public feeling was so aroused that the substitute measure prohibiting importation and permitting free exportation had to be temporarily discarded. At the end of the session of Congress, when the feeling had subsided a similar measure was introduced and unostentatiously passed. It prohibited the importation of the old coins and permitted their free exportation. The free importation of American silver was not disturbed.

The Government of Honduras, since it receives the old silver money in its offices at the legal rate of two pesos to the dollar, received a large part of its revenues in silver money. This was most evident in the custom houses on the North Coast where the silver was especially in disfavor. Accordingly in March 1921 a bill was passed not going so far as did the former circular of the Minister of Finance, but which made at least fifty per cent of the custom duties payable in American money and authorized the Executive to amortize the old silver coins at the rate of two to one. The Government shipped a certain amount of the silver to the United States and sold it as bullion, suffering a loss of about 25 per cent. Due to this loss the process was not long continued.

In spite of the law against its importation, clandestine importation of the silver took place. As the amount of silver in circulation

increased, the ratio of two to one between local silver money and American money has not been universally maintained. On the North Coast where American money has long been the customary currency the merchants insist on receiving American money, or if silver money is accepted, it is taken at varying rates of discount. The merchants are willing to receive it only because they are allowed to pay half of their custom dues in silver. This privilege provides a use for the coins which helps to counteract depreciation.

2. *Exodus of American money*

Large quantities of American money have been exported since the first of 1921 when the old silver coins became a part of the currency. However, the exportation of the American money was not caused entirely by the reappearance of the silver coins. During the period of boom and prosperity when the price of silver was high, imports increased very greatly as noted above. Merchants were making good profits and bought heavily of foreign commodities. Then came the depression and prices began to fall. As in the other Central American countries the merchants discovered that they had bought excessively, and found themselves overstocked with goods, the prices of which were falling but payment for which had not yet been completed. In December 1920 exchange rates went to a premium of two per cent which represents approximately the "gold point" for the exportation of American money. Exports are generally less during the period of from November to April and less drafts are offered for sale. The situation was intensified by the closing of the Rosario mine in April 1921 on account of the low price of silver.[1] The drafts of this company form a large portion of those offered in Tegucigalpa.

Since imports were greatly increased, and at the same time the

[1] The recovery in the price of silver from its extreme low points enabled the Rosario mine in the spring of 1922 to resume operations.

principal source of drafts in the southern part of the country was cut off, exchange rates went to the gold export point. Also the amount of the currency was increasing due to the return of the silver money, which increase tended to raise exchange rates. American money, which was more valuable than native money, and being largely paper and the most easily exported, was naturally shipped out of the country, and returned to the United States where drafts could be drawn against it. American money was exported in large amounts in spite of the prohibition of export which was imposed by a strained interpretation of the law of February 1921 permitting the free exportation of the old silver coins. The exodus of a considerable amount of American money thus would have taken place had there been no increase in the currency through the reappearance of the silver coins.

The premium on drafts on New York went to three per cent in June 1921, i.e., $100 for 206 pesos gold, and by the end of the year most of the American paper and much of the American silver had been exported from Tegucigalpa and the interior of the country.

Outside of Tegucigalpa and the North Coast American money has practically disappeared from circulation. It remains in Tegucigalpa, the capital, because of the law requiring that fifty per cent of the customs duties be paid in American money. The money is transferred from the custom houses on the North Coast to Tegucigalpa at par by the Banco Atlántida according to a contract of March 1921 between the bank and the Government. The Government pays out the money for salaries and other expenses in Tegucigalpa, and it is then received by the merchants who deposit it in the Banco Atlántida to establish credits with which to buy drafts on the United States. Some of the merchants advance funds to the Government in silver money against the custom receipts as security which are received at the end of the month, and then receive back American money in return.

A peculiar situation exists and the country really has a dual currency; in a sense it has both the gold standard and the silver standard at the same time. Aside from the North Coast and Tegucigalpa the country is practically on the silver standard, and American money is rarely seen. Outside of these two sections the banks are reluctant to make payments in American money owing to the difficulties in obtaining it. The market for the purchase of drafts with the old silver money is not very broad, but the rate of exchange for silver money has fluctuated between 205 and 235 pesos for $100.

On the North Coast the currency is almost exclusively American money; in Tegucigalpa it is about three-fourths domestic silver and one-fourth American money, the silver being at a discount in terms of American money. In the remainder of the country the currency is almost exclusively domestic money.

It is probable that the situation is more or less transitory and that unless there is positive reform the country will either go back to the silver standard as it prevailed before the war, or that the old money will become adjusted to American money, and as fiduciary money become a part of the gold standard. If the Government should guarantee the silver money, or if confidence in it should be restored, it would be treated as fiduciary money, and unless it proved to exist in an excessive amount, would circulate on a par with the American money. The American money in the country might be looked upon as an elastic element in the currency to take up the slack in the balance of payments in the foreign trade. In order to assure the permanency of the gold standard, however, the arrangement is unsatisfactory since in a year of poor exports the American money might all leave the country.

On the other hand, if the price of silver should rise, and should rise sufficiently high, the old coins would be withdrawn from cir-

culation and be replaced again by American money. When the price of silver is at seventy cents an ounce the coins are worth approximately fifty cents, the legal rate. The accompanying table shows the course of silver prices since 1910. It is to be regretted that the silver coins were not demonetized when the price of silver was high and when they were not in circulation, as was recommended in the early part of 1920 by the Minister of Finance.

PRICE OF SILVER

Average price per fine ounce in New York

IN DOLLARS

1910	.541	1914	.553	1918	.984	1922	.671
1911	.539	1915	.519	1919	1.120	1923	.669
1912	.615	1916	.686	1920	1.019		
1913	.605	1917	.895	1921	.631		

	1920	1921	1922	1923	1924
January	1.339	.664	.659	.661	.639
February	1.327	.598	.657	.647	.647
March	1.237	.567	.648	.680	.643
April	1.201	.598	.671	.673	.644
May	1.035	.603	.716	.675	.659
June	.928	.591	.716	.652	.670
July	.929	.608	.707	.634	.675
August	.969	.621	.698	.632	
September	.945	.662	.699	.645	
October	.842	.714	.684	.639	
November	.785	.685	.655	.641	
December	.655	.661	.643	.650	

Data taken from the Annual Report of the Director of the Mint.

3. *Monetary reform*

THE present situation in Honduras is unsatisfactory. In addition to the uncertainty as to what may take place in the future, there exist the difficulties from having the currency made up of two

classes of money which are not in accord with each other, two elements in the currency which are subject to different economic forces. Where American money and the local silver circulate together, unnecessary confusion in making change exists.

The "real" which is one-eighth of a peso and equivalent to six and one-quarter cents in American money, at a two to one basis, is a common unit of account. Pieces of one real have mostly ceased to circulate although a large number of pieces of two reales are in circulation.

A detailed plan for monetary reform, drafted by Dr. Arthur N. Young, Financial Adviser to the Government of Honduras, and presented to Congress in February 1921, provided for a national monetary system, to be based on a form of the gold exchange standard. Although Honduran gold coins were authorized, the plan was to have American paper or gold money form the basis of the system, while the fiduciary currency would consist of national money, guaranteed by a reserve of at least thirty-five per cent to be kept in the United States for the purpose of redeeming the fiduciary coins at par plus a premium approximately equivalent to the cost of shipping American currency. A translation of this project is given in the appendix. The unit was to be the peso oro similar in weight and fineness to the American dollar to which the country has become accustomed. The fiduciary coins were to be similar to those of the United States with an additional copper coin equal to one-half of an American cent, or equal to the Honduran centavo. The project was approved by the leading business interests and by the principal members of the Government, but was not favorably acted upon by Congress due chiefly to unfortunate political complications combined with temerity for reform and a lack of understanding of its provisions.

PART IV NICARAGUA

Chapter XII

MONETARY HISTORY PRIOR TO 1911

1. *Early monetary history*

THE early monetary experience of Nicaragua was similar to that of the other Central American countries. Under the Spanish régime the monetary system was based on that of Spain although the actual currency in circulation was a polyglot mixture of various coins, also commodities, differing from one district to another. In some sections cocoanuts passed from hand to hand as money, as also did cacao beans. The metallic money was partly from Spain and partly from South American countries. The coins were not of a uniform character and many were crudely minted. Much of the currency consisted of the "macacas" or "macuquinas," which were irregular pieces of silver cut to the proper size and bearing the official stamp.

The advent of the republic in Central America brought but little change in the currency system in Nicaragua. A legislative decree of January 1826 declared that the public offices would receive all the money of good quality that circulated before the revolution including the "moneda macuquina." Money of inferior quality the Government would not accept. That there was a fair amount of this inferior money in circulation at the time is indicated by the numerous dispositions dealing with the problem. The coins appear to have been counterfeited, clipped and plugged to a large extent, and this was the source of much confusion. The difficulties became especially troublesome about 1835 and the years following. Public employees would receive the better grades of money and quietly substitute it for money of inferior quality which they were able to buy cheaply. In the hand to hand circulation the people dis-

criminated as to the coins accepted. This confused transactions, so that the Government specified certain coins and declared it unlawful to refuse to accept them at the regular values, imposing a penalty on any who disobeyed.

As an example of the efforts of the Government to introduce order into a disorderly currency system the following is a translation of a decree issued in January 1840. It is typical of the dispositions of the time, and shows the complicated state of affairs: "Since an examination of the money of Peru, Bolivia, Arequipa and Cuzco shows it to be of inferior quality, eight reales of this money being equal in value to five and three-quarter reales of our other current money, it is decreed that, (1) Money of Arequipa of four reales coined in 1838, that of two reales of 1828, and of one-half real of 1837 be received for three-quarters of its nominal value. The same shall prevail regarding the reales, the four reales and the twelve reales coined in Bolivia since 1830, and regarding the four reales and twelve reales of Peru and Chile since 1835. (2) The 'pesos fuertes' of these republics, not being found inferior, shall circulate at their nominal value."[1]

In view of the numerous foreign coins of various values circulating in Nicaragua the Government frequently posted a table giving the comparative values at which the different moneys should circulate, and at which the Government offices would receive them. Certain coins badly mutilated or debased were prohibited from circulation entirely.

Nicaragua endeavored to maintain the bimetallic standard of the Spanish system whereby sixteen silver pesos were equivalent to one gold onza, but due to the bad condition of the silver money, the more valuable gold money was driven out and during this early period there was very little of it in circulation. Furthermore,

[1] Nicaragua; *Código de la Legislación;* Executive decree, January 27, 1840.

the wealth of the Nicaraguans was not great, and the small value of the silver coins answered well for the ordinary transactions, so that there was little use for the more valuable gold coins. The onzas which circulated did not always pass at a fixed value of silver money. Around 1845 they were commonly circulating as the equivalent of seventeen silver pesos although they were originally supposed to be the equivalent of sixteen pesos. The fluctuating relationship between the market value of gold and silver contributed to break down the joint circulation of the two metals. The gold price of silver rose beginning about 1850, and as a result the gold onzas became somewhat less valuable in terms of the silver pesos. Furthermore, many of the gold onzas of the Latin American countries were underweight so that in 1861 Nicaragua declared that the onzas of these countries were to be received at a value of 15.60 pesos "fuertes." Two years later, since these onzas were circulating in the other Central American countries at the value of sixteen pesos "fuertes," Nicaragua declared that she would receive them at this value.

In 1878 there was need for more small money and Nicaragua commenced the coinage of the copper centavos equal to one hundredth part of a peso. Previously the peso was divided into eight reales, and the small coins were silver reales, or multiples and fractions of the real. The real was now worth twelve and one-half of the new centavos. The centavos were to be three-quarters copper and one-quarter nickel and were legal tender only up to twenty centavos.

2. *Beginnings of paper money*

The paper money régime, which under the government of Zelaya resulted so disastrously to the country, had its earliest beginnings in the latter part of the seventies and the first part of the eighties. Government paper money, "Billetes del Tesoro," as the notes were

called, was issued from time to time, and being issued in moderation circulated along side of the metallic money. The notes were redeemable in gold or silver but were not themselves legal tender, until a decree to this effect was issued in 1885. The chief difficulties from paper money at this time appear to have been those of counterfeiting which was so relatively easy that the Government several times found it necessary to recall the outstanding notes and replace them with new ones.

A banking law, promulgated by executive decree, was issued in March 1882 and arranged for the issuing of notes by banks. The Government discontinued issuing notes, and in 1887 granted a concession to the Bank of Nicaragua by which the bank enjoyed the exclusive right of emission. This concession was to last for a period of twenty-five years. The notes of the bank were not legal tender.[2] The bank issued a large amount of these notes, which were redeemable in coin at the will of the holder, and all went well until the new government, which had come into power as a result of the revolution in 1893, authorized in September 1894 the issuance of one million pesos in "Billetes del Tesoro Nacional."

This policy of the new Government the bank took exception to as a violation of its charter which gave it the exclusive privilege of issuing notes. The government notes were not redeemable in coin on demand as were the bank notes, although the government notes were supposed to have a metallic reserve of at least 25 per cent behind them, with the result that the government notes went to a discount in terms of the bank notes. Then, in accord with Gresham's law the notes of the Government began to drive from circulation the better notes of the bank.

[2] An exception to this existed for a short time in 1893 when the notes were declared legal tender during the revolution of this year, a revolution which ended the only period of peace and relatively good government which the republic had ever experienced.

To counteract a diminution in the value of the revenue on account of the payment of government dues in the depreciated notes, an order was issued in 1896 that a specified portion of the government dues be paid in coin. The bank contested its legal position in regard to the notes, but to no avail. The final blow to the bank notes came in September 1897 when the Government prohibited all government officials receiving funds to accept anything but gold, silver or "Billetes del Tesoro Nacional," except with a discount of ten per cent, and imposed a penalty on any who departed from this rule. This measure was followed in a few months by an authorization for a large increase in the amount of government notes.

The bank endeavored strenuously to defend its charter rights to exclusive emission, but was unsuccessful and its notes were gradually retired from circulation. A few days before the decree was issued in September 1897 the bank's circulation amounted to 615,000 pesos; by the end of the year this had fallen to 320,000 pesos, and by the end of 1898 had fallen to 82,000 pesos. The bank's circulation continued to decline until there was only a nominal amount outstanding. Its place was taken by the increasing issues of government paper.

3. *Depreciation of Government paper money and disappearance of silver coin*

THE government notes began to depreciate from the very beginning, but during the early years the depreciation was not very great. By 1902 the depreciation had affected the Government's revenues so that the Government now declared import duties were to be paid with a charge equal to the depreciation of the bills as indicated by exchange rates for gold. This measure amounted to putting the Government's revenues upon the gold basis, although the country was in fact upon the silver basis, and the paper money was in process of reducing it to a paper basis; in fact the country

might be said to have been upon the paper basis then since the circulation of the silver money was greatly reduced and the coins were at a premium in terms of paper.

The silver currency at this time was similar to that of the neighboring countries, a collection of coins from various places, chiefly Central and South American countries. The silver peso was one of about 25 grams .900 fine. The gold price of silver had been continually falling over a period of years, and exchange rates for gold were thus rising independently of the depreciation of the paper. If the price of silver in foreign markets were sixty cents an ounce, the value of the silver peso in American money would be about forty-three cents. Exchange rates were quoted in terms of the number of pesos to $100 so that if the peso were at a value of fifty cents—a price of silver of about seventy cents—the rate would be quoted at 200; a rate of 250 meant a value of only forty cents for the peso. The price of silver for 1902 averaged about fifty-three cents an ounce, which gave a gold value of about thirty-eight cents to the silver peso and would mean a normal exchange rate of about 265. However, the exchange rate for paper pesos for 1902 averaged about 370, indicating a gold value of only about twenty-seven cents for the paper peso, or a depreciation of nearly thirty per cent.

The issues of government paper continued to grow with the result of increasing depreciation. President José Santos Zelaya, who ruled Nicaragua with almost absolute authority for sixteen years, until deposed in 1909, exploited the country for his personal profit and found the expedient of paper money a convenient way to raise revenue. Another of his methods for securing revenue was to sell valuable concessions or monopoly rights to private individuals, until almost all forms of enterprise were burdened with tributes which had to be paid someone. The abuses of Zelaya's rule are not

dissimilar to those of Estrada Cabrera's in Guatemala. In both instances a long period of harsh misgovernment was accompanied by inflation of the currency through issues of paper money.

The following table will show the amount of notes issued and the amount outstanding at the end of each year until 1912 when currency reform was inaugurated.

Issues of Paper Money in Nicaragua

YEAR	NEW ISSUES	NET OUTSTANDING DEC. 31	AVERAGE RATE OF EXCHANGE (*Selling rate for American gold, pesos per* $100)
1895*	*P* 271,650	*P* 271,625	197
1896*	221,875	493,500	191
1897	500,268	993,768	207
1898	1,521,000	2,379,642	219
1899	376,355	2,691,304	215
1900	658,882	3,299,935	208
1901	2,200,624	5,355,822	372
1902	3,000,000	8,306,235	528
1903	——	8,082,065	720
1904	——	7,931,905	684
1905	——	7,801,905	616
1906	235,000	7,896,905	540
1907	1,015,000	8,865,154	630
1908	1,850,000	10,671,153	797
1909	1,499,950	12,149,103	913
1910	19,625,000	30,952,103	1,150
1911	24,470,000	48,557,103	1,800 (approximate)

*To October 12. Data compiled by F. C. Harrison and Charles A. Conant; Plan of Monetary Reform for Nicaragua, April 1912. Exchange rates 1895-1900 from Report of the Collector-General of Customs, 1911-13, p. 58.

It can be seen that during the first few years of Zelaya's rule emissions were made in only moderate amounts. Until the end of 1897 the new issues exceeded only slightly the suppressed issues of the Bank of Nicaragua. Also the silver coin which was driven from circulation is to be deducted from the total currency of the country, so that in spite of the new issues of government paper money the net currency of the country was not as greatly increased during the first five or six years as might be expected. Thus depreciation was not very great at the outset.

The years 1901 and 1902 were years of turmoil when extra revenue was needed to put down revolutions, hence the circulation was increased during these years. Exchange rates mounted rapidly. The difficulties brought about by excessive issues of paper money caused the Government to refrain completely from any new issues during the next three years. In 1906 a small amount was put out, but this amount was not sufficient to replace the notes that had been cancelled so that the net circulation actually declined. There resulted a material fall in exchange rates.

The years 1907, 1908 and 1909 were years of revolutionary uprisings finally culminating in the overthrow of Zelaya. Large additions to the paper currency were made during these years and exchange rates rose sharply. In January 1907 the rate averaged about 510. It rose steadily from this time until in April 1909 it was over 1,000, or ten pesos to the dollar. In these three years the note circulation increased over fifty per cent. But this proved to be but the beginning of still more reckless inflation which ensued in the next two years.

The familiar silver money began to disappear from circulation soon after the paper became depreciated, and by 1902 or 1903 there was very little of it in evidence. Some was hoarded but a large part was exported to Honduras and Salvador where it still passed

currently. In Costa Rica the old silver money was replaced by national money redeemable in gold. Some of the old silver coins still existed in Guatemala at this time, but the same events were taking place in Guatemala as were taking place in Nicaragua, and the silver money there also was being driven out by increasing issues of paper. The chief countries to which the silver went when it left Nicaragua were Honduras and Salvador.

On the east coast of Nicaragua the paper money of Zelaya never gained much of a foothold nor circulated freely. Nicaragua resembles Honduras in the way the territory bordering on the Caribbean is separated by geographical barriers from the interior and Pacific dictricts. Neither of these two countries have transcontinental railways as do Guatemala and Costa Rica. Furthermore the trip to the Caribbean seaboard is a long and arduous one, and the means of transportation are uncertain, so that there is little communication between the two coasts. The Caribbean towns which have been developed by the American fruit companies due to the fecundity of the territory in the growing of bananas, have become Americanized and are very different in character from the native Central American towns with which the towns of the Caribbean coast have little in common, although they are under the same government. In Bluefields, which is on the east coast of Nicaragua in the banana country, the silver money remained in circulation when the central and western sections of the country were upon the paper basis. Zelaya was unable to impose upon the people of the eastern coast all of the arbitrary measures which the rest of the country endured. The paper was in disrepute there and the people insisted on receiving metallic money. Much of the silver which left Managua and the other western cities when paper dominated there, found its may to the eastern coast of Nicaragua as well as to the republics of Honduras and Salvador.[8]

[8] American money was also in circulation on the eastern coast of Nicaragua.

The Government endeavored to prevent the silver from leaving the country by passing a law in 1903 prohibiting its exportation. However, the following year, 1904, this law was repealed, although a tax of two per cent gold was placed upon all exportations of silver coin. In 1906 this tax was repealed so that the exportation of the silver coin was then both free and untaxed.

One important effect of the depreciation of the paper money was to cut down the values of the Government's income. Various measures were adopted to counteract this. We have already noted the order in 1896 that a certain portion of the Government dues was to be paid in coin, also the decree of 1902 that in collecting import duties an extra charge was to be collected equal to the depreciation of the notes. In 1904 it was decreed that all customs dues were to be paid in United States gold coin or prime drafts on the United States, or if the debtor chose he might pay the equivalent in national paper money at the current rate of exchange. This was modified in 1905 when the policy was adopted of declaring a definite rate for the paper. In February 1909 a rate of five pesos to the dollar was officially recognized as the rate for receiving the paper notes. This was raised at the end of 1909 to 6.50. These rates were somewhat below the current exchange rates, but general prices and wages lagged behind the depreciation as shown in exchange rates, so that the expenses of the Government expressed in the paper money, did not increase as rapidly as did exchange rates which were rising sharply.

An interesting study from the standpoint of monetary theory is found in comparing the gold values of the total currency at the ends of the different years. The following table shows the gold value of the circulation expressed in terms of United States dollars.

Gold Value of Total Paper Currency of Nicaragua on December 31

YEAR	CIRCULATION	RATE OF EXCHANGE	GOLD VALUE (*in United States dollars*)
1901	*P* 5,355,822	400	$1,338,900
1902	8,306,235	595	1,396,000
1903	8,082,065	700	1,154,500
1904	7,931,905	645	1,229,700
1905	7,801,905	628	1,242,300
1906	7,896,905	520	1,518,600
1907	8,865,154	700	1,266,400
1908	10,671,153	875	1,219,500
1909	12,149,103	975	1,256,300
1910	30,952,103	1,200	2,579,300
1911	48,557,103	1,800	2,697,600

The gold value in the right hand column is obtained by dividing the total circulation by the rate of exchange. It will be noticed that until 1910 there was not much variation in the gold value although the amount of currency had more than doubled since 1901. This uniformity in value is what would be expected, since unless there is an increase in the volume of business to be transacted, an increase in the amount of currency would mean that each unit would have a smaller share of the money work, or in other words have a smaller fraction of the total value attach to it, and the total value of the currency, expressed in terms of gold for example, would remain unchanged. Exchange rates fluctuate so erratically and are subject to so many uncertain market conditions that they are an imperfect index at any one time of what the gold value of the money unit will be when readjustment is complete. Especially is this true when inflation and depreciation have been very rapid, as was the case with the German mark. Hence differences in the right hand

column occur, and only general uniformity is to be expected. There is evident, however, a tendency toward proportional increases in exchange rates accompanying increases in the currency. If this relationship were absolutely proportional the gold value of the total currency would be constant.

The enhancement in the gold value of the circulation in 1910 and 1911, years of great inflation, shows that the exchange rates did not adjust themselves immediately to the larger amount of money in existence and did not reflect immediately the full effect of inflation. The result of this lag was an apparent rise in the value of the total currency. Also, encouraging prospects for the future and for an end to excessive paper money tended to prevent the rates from rising to heights that they might otherwise have reached. When the circulation advanced from twelve million in 1909 to nearly thirty-one million in 1910 exchange rates should have risen to around 2,300 in order to maintain a constant gold value for the total. Again in 1911 when the currency mounted to over forty-eight million pesos a corresponding exchange rate would be about 3,600. The fact that the rates were considerably below these levels indicates the friction and slowness with which business and the economy of the country as a whole adjusted themselves to new inflation. Furthermore, once the money of a country is redundant in the extreme, every new addition is apt to have an effect disproportionate to the actual amount of increase, due to the extreme adjustments necessitated by the great amount of currency.

The rise in exchange rates in 1903 was due largely to revolutionary disturbances which disturbed business and reduced the monetary demand, rather than to an increase in the circulation which actually declined this year due to the incineration of about 224,000 pesos and no new emissions. The circumstances surrounding the great additions to the currency in 1910 and 1911 are discussed below.

Chapter XIII

FALL OF ZELAYA; AMERICAN INTERVENTION AND FINANCIAL ASSISTANCE[1]

1. *Zelaya deposed*

CONDITIONS in Nicaragua under the tyrannical power of Zelaya became increasingly difficult. His policy was one of terrorization and oppression. The practice of granting concessions and special privileges was carried to the extreme until most forms of enterprise were no longer free. Unscrupulous promoters were given special grants which were injurious to the country at large, although lucrative to their owners. The discontent caused by the abuses of Zelaya's rule led to a state of almost continuous revolution. In the last ten years of his power there were no less than sixteen armed uprisings, culminating in the revolution of 1909 by which he was finally overthrown.

The revolution started in the fall of 1909 on the east coast of Nicaragua, where sentiment against Zelaya was especially bitter due to concessions recently granted which injured the interests of the people in this section. Particular discontent was caused by an exclusive right given to one company to operate a line of steamers on the Bluefields River. The foreign colony, which dominated the east coast, was thus friendly at the outset to the revolution, and lent assistance in the form of money and supplies to the Nicaraguan Conservatives who were organizing the attack against the opposing Liberal party which was in power in Managua, the capital. The

[1] A brief survey of the political situation is given here to serve as a background for the financial reforms which followed the overthrow of Zelaya and the accession of the Conservative Party into power. For a fuller treatment cf. Munro, Dana G., *The Five Republics of Central America*, Oxford University Press, 1918.

difficult character of the country between Managua and Bluefields, forming as it does a barrier between the east coast and the rest of the country, afforded protection to the revolutionists, enabling them to organize their forces and set up a government in Bluefields before the government in Managua could offer effective resistance. The leader of the revolutionary forces was Juan J. Estrada who had been governor on the east coast. He was now declared provisional president of the *de facto* government.

The revolutionary forces proceeded inland, but met with little success in their attempt to take over the western cities, and after a severe defeat Estrada was forced to retire to Bluefields from whence he came. After this defeat of Estrada the government troops made preparations to attack Bluefields, and very possibly would have stamped out the rebellion at this time had not the United States intervened.

Friction between the United States and the Government of Nicaragua had been developing for a period of years. The rule of Zelaya was becoming increasingly tyrannical, and he was having less and less regard for the rights of Americans in the country. His attitude toward the American Government was defiant, and his treatment of the American Minister in Managua discourteous. He was continually conspiring against the other countries of Central America in order to put his friends in office there, and thus kept Central America in a state of war and turmoil until practically the whole isthmus had turned against him. He violated the agreements reached at the Washington Conference of 1907 when the five republics of Central America entered into conventions which were aimed to avoid wars and revolutions in these turbulent countries. A general treaty of peace and amity was signed there to provide co-operation and harmony in the furtherance of their common interests. The Washington Conference had been necessitated largely by the aggres-

sive designs of Zelaya and the hostilities which resulted therefrom. The Governments of Costa Rica, Salvador and Guatemala now made representations to the United States protesting against the actions of Zelaya and his repeated disregard of the Washington conventions.

The revolution in 1909 against Zelaya thus enjoyed the sympathy of the United States as well as of the countries of Central America where he was fomenting revolutions and preventing the establishment of peace. He had long been the chief disturbing element in the isthmus. Several other unpleasant incidents helped produce the strained relations between Zelaya and the Government in Washington. The climax was the torture and execution by Zelaya of two American citizens, Roy Cannon and Leonard Groce, who were officers in the revolutionary army, which fact, however, Secretary Knox said did not preclude their being "dealt with according to the enlightened practice of civilized nations."[2] After repeated outrages the United States broke off relations with Zelaya's Government and openly supported the revolution which the State Department declared "represents the ideals and the will of a majority of the Nicaraguan people more faithfully than does the Government of President Zelaya."[3] The Secretary of State sent a note to the Nicaraguan Chargé d'Affaires at Washington which recounted the abuses of Zelaya's régime and the outrages culminating in the killing of the two American citizens, and which stated that since the United States could no longer feel respect and confidence for the Government of Zelaya, it was not appropriate to maintain diplomatic relations with it.

This note of Secretary Knox sounded the death knell of Zelaya since he knew that he could not long maintain himself against the

[2] cf. *United States Foreign Relations*, 1909, Nicaragua, p. 456.

[3] *Ibid.*

opposition of the United States. He attempted a reconciliation, but finally, under pressure from President Díaz of Mexico and his friends locally, turned over the Government to Dr. José Madriz, a respected private citizen and a member of Zelaya's party, thus hoping to regain the friendship of the United States by appointing a man of known integrity and at the same time retain the power for the Liberal party to which he belonged. However this coup was unsuccessful since recognition of the new Government by President Taft was not forthcoming.

This was the state of affairs when the Government in Managua attempted to attack Bluefields and wipe out the revolt at its source. The Nicaraguan Government had purchased a British vessel, the *Venus*, in New Orleans, and fitted it up with war equipment with the intention of blockading Bluefields. It sailed from New Orleans disguised as a merchant vessel and with its real purpose unknown to the authorities at New Orleans. At the beginning of the revolutionary trouble American warships had been ordered to Bluefields, and when the *Venus* arrived the Commander of the American cruisier *Paducah* refused to permit the vessel to interfere with American ships and trade, and thus carry out its plan of blockade. The *Venus* then sent word to Estrada that at the expiration of twenty-four hours it would bombard the town and take possession. The American Commander forbade this on the ground that such a bombardment and fighting would destroy the property of Americans and other foreigners. This action of the American Commander prevented the Government from striking a severe blow against Estrada and probably regaining the east coast. The government troops which had come to assist in besieging the town were not able to maintain themselves so far from home in the unhealthful climate, and soon were forced to retire.

Estrada thus was left unmolested and he mustered his forces and

again marched inland. The Government in Managua by now had met with reverses, and on his second trip Estrada was successful. In August 1910 he captured the city and took possession of the Government for the Conservatives. Five months later a constitutional convention met and elected him provisional president. His Government was forthwith officially recognized by the United States, about one year and a half since the first of the trouble.

2. *Financial intervention by the United States*

THE new administration was not strong, nor was it free from dissension within its ranks. Furthermore, the newly acquired power was not wisely used by the Conservative rulers. When Dr. Madriz handed over the Government to Estrada the Treasury was well filled. This money was looked upon as a fine prize to be divided up among the prominent Conservatives, and the money was paid out to compensate for injuries suffered under Zelaya or for whatever purpose ingenuity might devise. Those participating in the revolution were well rewarded for their trouble, either in cash or in land.

The treasury was soon depleted and resort was had to further issues of paper money which had proved such a lucrative source of revenue for both Zelaya and Dr. Madriz. Shortly before his fall Zelaya had placed large orders for notes with the American Bank Note Company, but as these notes were not received fast enough to meet the pressing needs, orders were given to local firms in Managua to supply seven million more notes. Part of these notes were issued by Zelaya, but most of them were put out by Madriz after Zelaya's fall. At the end of 1909 when Zelaya retired from office the total circulation amounted to slightly over twelve million pesos. At the end of 1910 when Madriz and later Estrada, had been in power, the circulation had risen to nearly thirty million pesos. There seemed no limit to inflation, and in the next three or four

months fifteen million pesos more were received from the American Bank Note Company of New York and thrust into circulation by Estrada. Only a small portion of the new money went to defray legitimate government expenses, and the bulk of it was distributed among the friends of the new Government who presented various claims for payment.

The administration of Estrada was not starting off auspiciously. The inflationary policy was disturbing to trade and exchange, and the general economic situation was extremely bad. Normal government revenues had fallen off decidedly, and political rivalries and disquietude within the ranks of the Conservative party itself weakened its power. With the Treasury practically bankrupt, and with the deposed Liberals causing trouble and awaiting an opportune time to strike, a general collapse seemed imminent. Disintegration and further turmoil were avoided only by the aid of the United States.

Payments on the foreign debt were in arrears and the creditors backed by their Governments were pressing Nicaragua for settlement. A great mass of claims of all descriptions was piled against Nicaragua. The administration, however, was not following a policy of rigid economy but was going the way of extravagant inflation unmindful of the consequences to the nation's finances and of the serious situation confronting the country. It soon became evident that action of some sort was necessary, and that if the United States desired to maintain the Monroe Doctrine and avoid intervention by a foreign power, it must itself take a definite stand and see that order and responsible government were maintained. If the United States did not see to it that Nicaragua fulfilled her contractual obligations, European powers were ready to assume this responsibility, and experience showed that once a European country intervened the new territory was soon apt to be considered a permanent possession.

In the latter part of 1910, shortly after the accession of Estrada, Mr. Thomas C. Dawson, American Minister to Panama, was sent by the United States Department of State to examine into conditions in Nicaragua, and to endeavor to bring about more unity and frugality in the local administration. Among other things he was to take up the matter of the numerous claims against Nicaragua and the question of a foreign loan. The result of his visit was the Dawson agreements signed in November 1910 by the different factions of the party which had come into power. In addition to the agreements of a political nature were ones looking towards the financial rehabilitation of the country.

Agreement number three of the Dawson agreements is quoted here in full since it marks the beginning of the participation of the United States in the financial affairs of Nicaragua. It is an agreement among the rival leaders of the controlling party.[4]

AGREEMENT NUMBER 3

"IN order to rehabilitate the public finances and to pay legitimate claims, both foreign as well as national, the good offices of the American Government will be solicited, with the object of negotiating a loan, which will be guaranteed by a certain per cent of the customs receipts of the Republic, collected in accordance with the terms of an agreement satisfactory to both Governments.

"Signed in triplicate at Managua.

JUAN J. ESTRADA
ADOLFO DÍAZ
LUIS MENA
E. CHAMORRO"

In view of this agreement the Knox-Castrillo treaty between Nicaragua and the United States was signed in June 1911. Early in the year 1911 Mr. Ernest H. Wands went to Nicaragua as Financial Adviser, and after making a survey of conditions reported the

[4] *United States Foreign Relations*, 1911, Nicaragua, p. 653.

situation to the State Department. The treaty between the two countries provided that the United States would help Nicaragua secure a loan from American bankers for the purpose of consolidating its indebtedness and for internal improvements which were urgently needed. A collectorship of the customs by a Collector-General was agreed upon to provide security for the loan. The treaty met with considerable opposition in the United States Senate, and in spite of its many friends was never ratified, due chiefly to agitation against "American Imperialism."

In the meanwhile the New York banking houses of Brown Brothers and Company, and J. and W. Seligman and Company had agreed to loan Nicaragua fifteen million dollars as soon as the treaty should go into effect. The money was to be used by Nicaragua for the refunding of its internal and external obligations, for the reform of the currency and for the construction of a railroad to the east coast. In order to carry out immediately the reform of the currency which was especially urgent, the Bankers and the Government of Nicaragua made arrangements for a temporary loan of $1,500,000.

3. *Mixed Claims Commission*

The so-called Mixed Claims Commission had its origin as a result of the Dawson Pact. The Commission was composed of three members, two Americans and one Nicaraguan, and its purpose was to investigate into the numerous claims outstanding against the Government. The Commission was provided for by a decree in May 1911, amended later, and began its labors immediately. It was to adjudicate without appeal all the unliquidated claims, especially those originating out of the abolition of monopolies, concessions and contracts of former Governments. Most of the claims grew out of the troubles of the past few years, although a fair amount were

for wars between 1893 and 1909. More claims were added by the war which came in 1912.

The Commission, with Judge Otto Schoenrich as president, worked for three and one half years during which time it passed on 7,911 cases, three of which were claims by the Government against concessionaires. Of the other claims which were against the Government the total claimed amounted to $13,808,000 in American gold. This was pared down by the Commission and the claims allowed were for a sum of $1,840,000. The majority of the claims were by Nicaraguans and for relatively small sums. Of the 7,908 claims against the Government all but ninety-one were based on damages and losses suffered as a result of wars and revolutions when cattle, horses, poultry, provisions and such things were carried off, or when houses were burned and looted.

Although the majority of the claimants were Nicaraguans, the amount claimed by Americans was greater than the sum total of all the other claimants as can be seen from the table below. The Americans, however, were awarded a smaller proportion than the other foreigners or than the Nicaraguans.

CLAIMS AWARDED BY THE NICARAGUAN MIXED CLAIMS COMMISSION[5]

NATIONALITY OF CLAIMANT	NUMBER OF CLAIMS	CLAIMED	AWARDED
Nicaraguan	7,491	$5,491,533	$1,217,650
British	149	152,541	24,427
American	66	7,576,654	538,750
German	34	49,174	16,693
Chinese	28	37,797	5,566
Italian	25	139,511	9,032
Spanish	21	135,349	2,697

[5] See Report of Nicaraguan Mixed Claims Commission to the Secretary of State of the United States, 1915; also article by Otto Schoenrich, president of the Commission, "The Nicaraguan Mixed Claims Commission," *American Journal of International Law*, 1915 vol. 9, pp. 858-69.

NATIONALITY OF CLAIMANT	NUMBER OF CLAIMS	CLAIMED	AWARDED
French	20	34,834	5,959
Colombian	17	38,554	3,160
Turkish	9	6,418	1,313
Costa Rican	5	42,079	1,576
Panamanian	3	10,174	8,110
Swiss	1	35,000	—
Guatemaltecan	1	16,000	—
Miscellaneous	38	41,543	5,499
Total	7,908	$13,808,161	$1,840,432

Opposition to the Commission on the part of the English, French and German ministers caused some embarrassment since these countries believed that the Commission was too much American and would discriminate in favor of American claims. However, inspection of the above table will show that the Americans received a smaller proportion than other foreigners or than Nicaraguan claimants. The reason that the Americans received a smaller proportion than the others was that most of the American claims were based upon the cancellation by the Government of concessions that were illegal, and the claims included large items for estimated future profits which the Commission would not allow. The claims of the other foreigners and the Nicaraguans were based largely on losses arising out of wars and revolutions, and the task of the Commission was to verify the loss and then to evaluate it. In its decisions the Commission was guided by a general set of rules which were adopted at the outset, and as a result all the judgments of the Commission were rendered unanimously.

The Government of Nicaragua accepted the awards of the Commission as binding, but since the loan treaty which was to provide Nicaragua with funds, failed of ratification in the United States, the country was unable to pay off these recognized debts. However, about $160,000 was turned over to the Commission from the cus-

toms receipts, and was used to pay off 4,600 of the smaller claims, mostly claims of natives who had suffered during the years of revolution.

4. *Collectorship of customs established*

The currency situation in Nicaragua was critical, so the Bankers agreed to loan the country $1,500,000 immediately in order to rehabilitate the currency and finances, expecting the United States would later ratify the Knox-Castrillo treaty of June 1911. The loan was effected in September 1911, and the Bankers received treasury bills which bore six per cent interest and which were to be repaid out of customs receipts. Included in the agreement was a provision that there be appointed a Collector-General of Customs, similar to the arrangement provided in the loan treaty which failed of ratification. The Collector-General was to be "nominated by the Bankers, approved by the Secretary of State of the United States, and appointed by the Republic."[6] Accordingly, Colonel Clifford D. Ham, a man of considerable experience in this field, was nominated by the Bankers, and after being approved by the Secretary of State in accordance with the agreement, was officially appointed by the President of Nicaragua in November 1911, and assumed his duties the following month. His position is thus a three cornered one.

The contract between the Bankers, Messrs. Brown Brothers and Company and J. and W. Seligman and Company, and the Government of Nicaragua arranging for the temporary loan, or the Treasury Bills Agreement as it was called, provided that the Collector of Customs should collect all the customs revenues, and after paying for the necessary expenses of collection, should dispose of the receipts as specified in the contract. The Government agreed not to alter the import and export duties or make any changes that would

[6] *Treasury Bills Agreement;* Article Fifth, Section 2.

affect the value of the customs revenues without agreement with the Bankers. In spite of its disadvantages a collectorship of the customs seemed the only way to secure funds for the financial reform in Nicaragua. With the country's previous record of default and turbulence no reliable banking house would sink money in Nicaragua without adequate guarantees.

A refunding operation of the country's foreign debt was brought about in May 1912 by the aid of the American Bankers. In 1909 Zelaya had refunded the foreign debt existing at the time, which dated back for a number of years, and had issued £1,250,000 in gold bonds bearing six per cent interest. The bonds were held by the Ethelburga Syndicate of London, and the money Zelaya received from them, in addition to redeeming or converting the old bonds, was to be used in the construction of a railway to the Caribbean coast, and for general government purposes. This was in 1909 shortly before Zelaya was dethroned. With the coming of the revolution and the overthrow of Zelaya the service of the loan was suspended and payments had not yet been resumed although the British Government was bringing pressure to bear for a readjustment. An agreement was reached in May 1912 between the American Bankers as agent for the Government of Nicaragua, and the Corporation of Foreign Bondholders acting on behalf of the British owners of the securities, whereby the interest was reduced from six to five per cent. Provisions were made that if the bonds were paid within certain periods a discount would be given. In return for these concessions the British bondholders were to have a first lien on the whole of the customs revenue, and an American Collector-General of Customs was to remain in office and collect the revenues so long as any of the bonds remained unpaid, remittances to be made through the New York Bankers.[7]

[7] These bonds had been a lien against the Ferrocarril del Pacífico de Nicaragua. This lien was now removed.

This refunding operation was thus favorable to Nicaragua as well as to the London bondholders since the added security of an American Collectorship of the Customs enabled Nicaragua to effect a saving of one-sixth of the annual interest charges by a reduction in the rate from six to five per cent. Nicaragua also received £371,000, which represented proceeds from the loan of 1909 which had not been turned over to her but which had been held in London when the service of the loan was discontinued. About one-third of this amount was retained in London to cover interest payments which were in arrears, and the rest was turned over to Nicaragua to be used in the reform of the currency and the payment of the country's obligations.

Customs Revenues of Nicaragua; Imports and Exports
(In terms of American gold)

YEAR	IMPORTS	EXPORTS	TOTAL FOREIGN TRADE	CUSTOMS REVENUES
1901	$2,265,000	$3,361,000	$5,626,000	$702,800
1902	2,170,000	1,933,000	4,103,000	506,400
1903	2,461,000	3,223,000	5,684,000	697,700
1904	3,202,000	3,926,000	7,128,000	910,600
1905	3,447,000	3,542,000	6,989,000	1,282,200
1906	3,409,000	4,231,000	7,640,000	1,595,200
1907	2,811,000	3,360,000	6,171,000	1,246,800
1908	2,959,000	3,648,000	6,607,000	1,027,400
1909	2,583,000	3,989,000	6,572,000	976,500
1910	2,856,000	4,545,000	7,401,000	854,500
1911	5,725,000	6,579,000	12,304,000	1,138,400
1912	4,967,000	3,862,000	8,829,000	1,265,600
1913	5,770,000	7,712,000	13,482,000	1,729,000
1914	4,134,000	4,955,000	9,089,000	1,234,600
1915	3,159,000	4,567,000	7,726,000	787,800
1916	4,778,000	5,285,000	10,063,000	1,036,100
1917	6,393,000	5,975,000	12,368,000	1,148,700

1918	5,930,000	7,755,000	13,685,000	997,200
1919	7,913,000	12,409,000	20,322,000	1,369,300
1920	13,864,000	10,787,000	24,651,000	2,055,100
1921	5,310,000	8,071,000	13,381,000	989,300
1922	5,124,000	7,903,000	13,027,000	972,100
1923	7,268,000	11,028,000	18,296,000	1,591,100

Data taken from Annual Report of the Collector-General of Customs, Nicaragua.

Chapter XIV

CURRENCY REFORM

1. *Preliminary events*

THE chief purpose of the temporary loan of $1,500,000 made in the fall of 1911 was to provide funds for a reorganization of the monetary system, and for the placing of the system upon a sound basis. Due to the unrestrained issues of paper money the condition of the currency was confused and immediate relief was needed. The banking houses of Brown Brothers and Company and J. and W. Seligman and Company, which were supervising the reform for the benefit of Nicaragua, appointed Messrs. F. C. Harrison and Charles A. Conant, men of wide experience in currency matters, to proceed to Nicaragua and work out a plan for monetary reform. They reached Nicaragua in December 1911 and immediately undertook their work.

Prior to this, in the fall of 1911, when arrangements regarding the currency reform were in progress, a surreptitious issue of ten million pesos was put out by the Government, even though the Treasury Bills Agreement of September first had already been signed and an understanding existed that there were to be no more issues of paper money. The issue was a breach of good faith and was also illegal since there was no official decree authorizing it. It was the Government's final stroke before reform was instituted and the lid went on. The money went largely to the friends of the administration, and brought the total circulation outstanding up to between forty-eight and forty-nine million pesos. A portion of the notes of the illegal issue was used to replace old notes that were dirty and torn so that they were unfit for circulation. Many of these old notes, especially the smaller denominations such as

the fifty centavo notes, were in an extremely dilapidated and filthy condition, and it would have been impossible for the Government to return them to circulation. Thus in 1911 6,865,000 peso notes were retired from circulation and incinerated, a large portion of which was the provisional notes that had been printed locally. In view of the renewed additions to the currency a written statement was obtained from the Government in January 1912 promising that there would be no further issues of paper money.

In June 1911, two days after the loan treaty with the United States had been signed in Washington, the Government of Nicaragua issued a decree declaring that the accepted rate between pesos and dollars should be twelve pesos to the dollar.[1] The futility of such a decree is apparent since the condition of the paper currency was unchanged and no provisions had yet been made for the maintenance of any gold parity. The optimism created by the prospects of American assistance to the weak and bankrupt country was responsible for the impression that now almost anything was possible and that economic laws were subordinate to statute laws. Also, the Government, realizing that its large issues of paper money had brought on the distressing condition of the currency and exchange rates, desired to reassure the people and bolster up matters. Thus it endeavored to legislate against exchange fluctuations, and avoid the discredit which attached to it for the emissions of fiat money. The decree perhaps had a salutary effect upon exchange rates temporarily since some people had faith in its potency or in the statement of the Government pledging the maintenance of a fixed rate. However fluctuations in the rates continued as great and as erratic as ever.

2. *Gold-exchange standard selected*

THE problem before Nicaragua had to do with the establishment

[1] *La Gaceta,* Nicaragua; June 23, 1911.

of some form of the gold standard. The gold standard as it exists today in the United States, for example, is an expensive luxury. A very large amount of gold is used solely to give us the benefits of the gold standard. Something over four billion dollars in actual gold at the present time is given over in the United States entirely to monetary purposes. In a backward country like Nicaragua a strong preference exists for metallic currency, and if any gold coins were struck they would be in great demand as against paper money with which the country has had sad experience. The gold would be used commonly for hand to hand circulation and hoarding, with resultant abrasion and loss. Money invested in gold for currency purposes yields no interest, except perhaps in the form of service rendered, and if it is possible to secure this service without the physical use of gold a net gain results. This end is accomplished by the gold-exchange standard as it has been employed successfully in India, Java and the Philippines. Certain aspects of the gold-exchange standard make it unattractive for large independent powers, but for small countries it offers many advantages.

Nicaragua is a small country with a population of only about seven hundred thousand people. Like the other Central American countries it is not a wealthy country, but one where wages and the standard of living are low. Since the cost of the monetary reform had to be met with borrowed funds, and the resources of Nicaragua were not great, the gold-exchange standard seemed the most economical and generally desirable system, the one best adapted to the country, at least for the first few years when she was being restored to a sound economic condition. The recommendations of the currency experts, Conant and Harrison, were for the gold-exchange standard, and it was this system that was later embodied into the law of March 1912.

The principle underlying the gold-exchange standard, in brief, is that by giving a country a fiduciary currency, either paper or metal, and arranging for the redemption of this money, not in gold locally but in drafts on a foreign country having the gold standard, which drafts can be converted into gold in the foreign country if need be and are thus at a parity with gold, the fiduciary currency at home is thus maintained at a parity with the foreign gold currency. A reserve fund is provided in the foreign country against which drafts can be drawn, and sold for local currency when exchange rates at home on the foreign country tend to rise, and the value of the local currency tends to depreciate in terms of the foreign currency. As the local money is paid in for the purchase of drafts due to the rise in exchange rates, it is withdrawn physically from circulation, the effect of which is to appreciate the domestic currency and thus restore the equilibrium in exchange rates. Conversely, if the value of the domestic money tends to appreciate in terms of the foreign money, so that exchange rates on the foreign country fall and rates on the home country rise, instead of gold being shipped to the home country drafts are bought, and as they are redeemed in the home country more of the domestic currency is paid out, which increase in the circulation continues and causes a fall in the value of the domestic currency until exchange rates fall to their normal level and the proper relationship with the foreign currency is again restored. Through this arrangement it is possible for a country to have its currency maintained at a parity with a gold currency and enjoy the benefits of the gold standard without having any gold within its own borders.

The salient feature of the gold-exchange standard is having a portion, if not all, of the reserve held abroad, and having redemption of the currency accomplished by means of drafts on this fund.

The seigniorage profits on the coinage of local silver are fairly

large and contribute an important amount in establishing the reserve fund in the foreign country. Also the reserve fund can be made to earn interest, when conservative management justifies such use of the fund. Another source of profit is from the sale of drafts in connection with the operation of the system. The premiums charged for drafts are small, and are supposed to be equal to what would be the cost of shipping the gold. Since the premiums are fixed and small, the fluctuations in exchange rates are confined within narrow limits similar to the "gold points" of a gold standard country. The sale of drafts in connection with the system does not ordinarily take place until the rates have gone either to the gold export or import point, and the system thus does not interfere with the exchange business of the private banking houses. Since the premiums on drafts against the fund are small, profits from this source are only moderate, but they are repeated again and again and in the course of time amount to a sizable sum. Thus in the course of time the system provides revenue which can be used either to increase the size of the fund or to pay for the expense of its establishment.

The original plan in sending the currency experts to Nicaragua had been for them to remain a few weeks in the country studying conditions, after which time they would return to New York and in collaboration with the Bankers prepare a plan for currency reform which would be presented to Nicaragua for adoption. However, they found it advisable to remain in Nicaragua until plans for reform were complete. In recommending the gold-exchange standard they recommended it only as a temporary arrangement, and believed that ultimately Nicaragua should have the simple gold standard. Their reasons for this were that the gold-exchange standard makes the country dependent upon a foreign country, and that Nicaragua as a sovereign state should have a system of her

own as soon as she possessed sufficient strength to do so and a Government of sufficient integrity not to exploit the currency. Also the gold-exchange standard opens possibilities for manipulation and mismanagement, and if improperly administered may break down. However, these disadvantages are apt to be magnified and in the case of Nicaragua the gold-exchange standard was the most logical and feasible one for an indefinite period; in fact there seem to be no reasons yet why a change to the gold standard would offer more advantages.

3. *Currency Law of March* 1912

THE details of the system worked out by Conant and Harrison were drawn up in the form of a law[2] which was approved by the National Assembly on March 20, 1912.

An important question to be decided was that regarding the size of the unit which was to be the basis of the new currency. The two units which were considered most seriously were, first that equal to fifty cents of American money, similar to the pesos of Mexico and the Philippines, and second that equal to the American dollar. The merits of the fifty cent unit were that it was close to the value of the old silver pesos with which the people were familiar before paper money drove them from circulation, and which still circulated on the east coast where the people refused to have anything to do with Zelaya's paper money; and also, the purchases of the Nicaraguans were mostly of small value and a unit worth fifty cents would be well adapted to their economy. A fifty cent unit is exactly one half of the American dollar and would not complicate exchange with the United States such as was the case in Costa Rica, for example, when the colón was made equal to a fraction over forty-six and one half cents. On the other hand a unit equal to the dollar

[2] The text of the law is given in the appendix, p. 236ff.

simplifies still further the exchanges and would facilitate trade and commercial relations between the two countries. It obviates the necessity of having two price lists by business houses, one in each currency. The dollar instead of the pound, franc, or mark, was the most appropriate unit for Nicaragua to conform to since the bulk of her foreign trade was with the United States. Imports into Nicaragua came very largely from the United States, England ranking second with exports to Nicaragua equal in value to only about half of those coming from the United States. Nicaragua's exports went to the United States, England, France and Germany, the coffee especially to France.

The government officials of Nicaragua favored a unit similar in value to that of the United States. After careful consideration the dollar unit was the one adopted.[3] The name given the new unit was the "córdoba," in honor of Francisco Hernández de Córdoba, the Spanish founder of Granada and León, two of the historic and important cities of Nicaragua.

The law provided for gold coins and gave the discretion as to the amount to be coined, of both gold and silver, to the National Bank, under regulations approved by the Executive. It was not intended, however, that any gold coins be struck. Nevertheless provision was made that whenever it should seem proper, upon agreement between the Executive and the National Bank, there might be unlimited coinage of gold. Provision was also made for silver coins approximately similar to those of the United States as regards silver contents; also for minor coins similar to those of the United States, with an additional coin, the half centavo piece equal to one

[3] The two units are usually said to be identical, but strictly speaking the Nicaraguan unit has a fraction more gold in it than the American dollar. It was given a gold content of 1.672 grams .900 fine; the American dollar contains 1.67181 grams .900 fine. For all practical purposes, however, the two units are identical.

half of a cent. It was planned to mint some coins of each of these denominations from the silver córdoba down, with the expectation, however, that the largest coin in general use would be the fifty centavo piece.

Article nine of the monetary law provides for the establishment of the Exchange Fund which was to be used in connection with the gold-exchange standard, and which was to form a part of the reserve against the notes of the National Bank, described below. The purposes of the Fund are given in the law and are described as follows: "To exchange on demand for the gold coin of Nicaragua and the notes of the National Bank of Nicaragua, in sums of not less than five thousand córdobas. . . drafts on the said Exchange Fund in the United Sttaes or other foreign country, charging a premimum of one half of one per cent for sight drafts and one per cent for telegraphic transfers."[4] The reverse of this was also specified, in substance: to exchange drafts on the National Bank of Nicaragua, on demand for currency of the United States or of any other country where a part of the fund may be deposited, in sums of not less than five thousand córdobas charging premiums similar to those given above. The Fund was also available "to make exchanges between the notes of the National Bank, the gold or silver coin of the Republic, the currency of the United States, and other foreign currencies, under regulations to be made for that purpose by the National Bank, subject to the approval of the Minister of Finance."[5]

The premiums charged for drafts may be temporarily increased or decreased by the Bank and may be different for different parts of the country, but they can never be higher than one and one quarter per cent for sight drafts and one and three quarters per cent

[4] *Monetary Law of March* 20, 1912, Article nine.

[5] *Ibid.*

for telegraphic transfers without the approval of the Minister of Finance. This fixes what corresponds to the "gold points" for a gold standard country. The amounts received as premiums from the sale of drafts or transfers are carried to the credit of the Fund.

The establishment of a National Bank was also provided for in the law as arranged by the Treasury Bills Agreement of September 1, 1911. The Bank was to be the fiscal agent of the Government and depository for the government funds. It was also to assist in putting into effect and maintaining the new currency system. The law provided for the exchange of the old national paper money for notes of the Bank on or before July 1, 1912, at a rate to be agreed upon between the Bankers and the President and not to be higher than fifteen pesos to the córdoba. Six months after the exchange was to take place the old paper was no longer to be legal tender nor received for public dues, but it might be redeemed under special regulations.

The importation of foreign coin, and the circulation of foreign currencies either paper or metal, was placed under the control of the Executive and he may permit it or prohibit it by decree. These are the more important provisions of the monetary law of March 1912. It contained various provisions relative to the installing and management of the new system, and repealed the Banking Law of March 1882.

4. *Installing the system*

One of the important matters to be determined in connection with the installation of the new currency system was the rate at which to stabilize the old paper money, i.e. what gold value to give the old paper when converting it into the newer currency. The chief guide in determining how many paper pesos to make the equivalent of one córdoba was the fluctuating rate of exchange between the

paper pesos and American dollars, which rate was indicative in a general way of the existing gold value of the paper money. Since business and the general economy of a country are much slower to adjust themselves to new currency conditions than sensitive exchange rates, the current rates of exchange were useful only as indicating a general tendency and were not to be taken absolutely. Furthermore, even though it were possible to determine accurately the existing gold value of the paper peso, it might not have been desirable to stabilize the peso at this value, but on the contrary greater justice to all concerned might have been accomplished by giving the peso a somewhat greater value than it possessed in its depreciated state, and in this way compensate to some degree for the loses sustained during the course of depreciation.

The Monetary Law did not definitely fix the rate to be adopted, but left the matter open, declaring that the old national currency should be exchanged "for notes of the bank, at a rate to be agreed upon by the President and the bankers and officially declared not less than three weeks prior to the date agreed upon, and in no event to be higher than fifteen hundred pesos in national currency notes for each one hundred córdobas."[6]

The selection of the conversion rate was a matter of considerable local interest and many of the merchants and business men expressed themselves as favoring a rate of ten to one. The rate finally selected was that of 12.50 pesos for one córdoba. The exchange rates for dollars at the time were in excess of this. They had been fluctuating between 1600 and 2000 pesos to $100. However, business had not yet had sufficient time to adjust itself to these changed conditions. The reasons for this belief were that the great increase in paper money and the great decline in the gold value of the currency were of recent date. An economic principle

[6] cf. Nicaragua, *Monetary Law*, March 20, 1912; Article Nine.

well established is that when depreciation takes place wages and general prices lag behind depreciation as reflected in exchange rates, wages and the prices of those articles which have conventional prices being the slowest of all. Custom is strong, especially in a backward country, and when the gold value of a currency is falling rapidly it is inevitable that wages and prices lag behind on their upward move. Popular resistance to higher prices encourages this lag. In Nicaragua there was no index number of prices nor of wages, yet it was evident that wages and prices had not risen in anything like the same proportion that exchange rates had risen.

The establishment of a rate of 1250 instead of one more in harmony with current exchange rates, would perhaps restore, it was hoped, to wages a portion of the purchasing power which they had lost in not being able to adjust themselves promptly to advancing prices and the depreciating money. At all events it was hoped that such a rate would at least halt a further loss to the workers. In the event that prices and wages should have already become adjusted to this level, or a level above this, a slight reduction in the level would give an advantage to the workers which would but compensate for losses already sustained, which advantage might be retained more or less permanently since wages were extremely low. Employers in general agreed that workers had suffered by the depreciation of the peso, and that if a rate of 1250 were so low as to give a slight advantage to the workers there probably would not result a reduction of wages in terms of the new money.

On the other hand, common opinion regarded the rate of 1250 as too high, rather than too low. There seemed to be considerable evidence that business had not yet adjusted itself even up to the point where 12.50 pesos equaled $1.00 gold, although current ex-

change quotations were very much in excess of this. Memorials were presented by leading merchants and business men from the different sections of the country recommending that a rate of 1000 be selected.

One of the arguments in favor of a rate of 1250 in preference to one of 1000, was that the latter rate gave a greater gold value to the peso and would entail a greater expense upon the Republic in redeeming its paper pesos than would a rate of 1250. The lower the value given the peso, the less expensive would be their redemption in córdobas. If 12.50 pesos were made the equivalent of one córdoba instead of 10.00 pesos, there would be a saving of twenty-five per cent in the conversion transaction.

On the other hand, the resulting increase in the gold value of the public revenue if the peso were given a high gold value, offered an advantage offsetting that resulting from giving the peso a low gold value. The foreign debt of the country was in terms of gold. The chief source of revenue was the customs dues, and the higher the gold value given the peso, the greater would be the gold value of the country's revenues.

Some sentiment was favorable to a rate of twelve to one. In June 1911 the government had issued a decree declaring a fixed ratio of twelve to one between national paper and American dollars. This decree and its futility have already been noted, but many people now looked upon the decree as a pledge of the Government, and held that the Government had committed itself to such a rate.

The plan for putting into effect the rate of 1250, which was the rate finally selected, was to reduce the volume of the currency outstanding by buying in a part of the paper at as favorable rates as possible, until the rate of 1250 should be attained. It was then planned to substitute for the old paper money, notes of the National Bank on the basis of 12.50 pesos for each one córdoba note. It was

estimated that a rate of 1250 would mean a circulation of about thirty million pesos. This was computed from the exchange rates of the past and the amount of circulation at the corresponding dates; thus when the circulation was about twelve million pesos the rate was 975, and when the circulation was about forty-two million pesos the rate was 1800. Assuming that a rate of 1250 meant a circulation of thirty million pesos (2,400,000 córdobas), there would need to be retired about seventeen million pesos since the total circulation was between forty-seven and forty-eight million pesos. However, Conant and Harrison believed that it would only be necessary to buy in about twelve million pesos and that these twelve million could be bought in at rates very much less than the prevailing exchange rates. The cost of buying in this paper was estimated to be about $780,000.

The loan for the reform of the currency under the Treasury Bills Agreement was for a sum of $1,500,000. The amount needed for the foundation of the National Bank was placed at $100,000. For the coinage of silver and fractional money to the amount of about $300,000 there was needed about $180,000, this would also cover the expense of recalling the old notes and issuing the new. In addition there was to be deducted from the $1,500,000 about $70,000 for various preliminary expenses. This left $370,000 for the establishment of the Exchange Fund which was to be the reserve for the notes, an amount which was considered insufficient for its purpose. The amount of paper money circulating at the commencement of the reform was expected to be equal to about thirty-five million pesos or two million eight hundred thousand córdobas. With this would be about three hundred thousand córdóbas in metallic currency, and against this total of three million one hundred thousand córdobas would be a reserve of $370,000, also the silver in the fractional currency which would be worth about $120,000, making a total reserve of nearly $500,000 or about sixteen per cent.

It will be remembered that a surreptitious issue of paper money was made in the fall of 1911 to the extent of ten million pesos. This unexpected issue added to the expense of the currency reform. Accordingly, in order to provide sufficient funds, the Bankers in March 1912 arranged a supplementary credit to Nicaragua of $500,000, to retire a larger amount of paper pesos and to increase the Exchange Fund. It was hoped the Fund would be built up gradually by profits resulting from the coinage of silver and other profits so that it would soon amount to forty per cent of the notes outstanding.

The process of reducing the currency from about forty-eight million pesos to an amount where an exchange rate of 1250 should prevail, began in the latter part of 1912. The selection of 1250 as the permanent rate was not announced until nearly the end of the year, so that speculation might be avoided as far as possible. A large part of the currency was bought in at the higher rates, which was cheaper for the government, but as the volume was reduced and the people were inclined to hold back their money waiting for more favorable rates, which it was believed would soon prevail, the rates began to fall. A large amount was secured at 1600, and also at 1500. Then on October 15, 1912, the Bank reduced the rate to 1400 where it remained until December 17, when it was reduced to 1350. On December 23 it went to 1300 and finally on January 13, 1913, to 1250. The following table shows the average rates of exchange for New York sight drafts during 1912, and how the rates were reduced in one year from 1800 to 1250, the permanent rate.

Rates of Exchange Between National Paper Currency and American Gold

(Pesos to the dollar)

1912		February	18.00
January	18.00	March	16.00

1912		September	15.00
April	16.00	October	14.00
May	16.00	November	14.00
June	16.00	December	13.00
July	15.50	1913	
August	15.00	January	12.50

(cf. *Nicaragua, Report of the Collector-General of Customs December* 1911 *to June* 1913, p. 62.)

The figures show how the rates fell steadily during 1912. There were no extreme fluctuations in the rates except during the first three months when the currency law had not yet been adopted. The rate of 1250 was attained January 13, 1913, but it was not until the latter part of March that the actual conversion by the Bank began. Silver córdobas were received and put into circulation in that month and also córdoba bank notes. As the coin and paper were put into circulation funds were put on deposit in New York with the United States Mortgage & Trust Company to secure the currency,[7] and thus the new currency system was started in operation, March 23, 1913.[8]

It was expected that all the paper pesos would be retired in the six months period ending September 23, 1913. However, this was not quite the case. On November 15, 1913, thirty-seven millions of the old paper notes had been withdrawn from circulation, and incinerated, either being bought up by the Government at varying rates or exchanged for new córdoba notes of the Bank. On this date, according to the computations, there were 9,500,000 of the old pesos outstanding. At the conversion rate of 12.50 these had a gold value of about 760,000 córdobas. The new córdoba notes in cir-

[7] Article 9 of the Monetary Law authorized the Minister of Finance to order the United States Mortgage & Trust Company, as trustee, to set aside funds in its possession for the establishment of the Exchange Fund.

[8] The Currency Law set July 1, 1912, as the date for conversion, but provided that a later date might be arranged with the approval of the Bankers.

culation at this time amounted to about 1,571,000, so the total circulation was estimated to be about 2,330,000. However, the old billete circulation was larger than had been anticipated, and on October 31, 1915, 49,415,000 pesos had been retired from circulation. The period for conversion was extended from time to time, but after November 1, 1915, only córdobas were received in the Government offices.

In installing the system various difficulties were encountered. The business interests of the western half of the country were favorable to the new currency; after their experience with the fiat paper money they welcomed a non-fluctuating unit. Nevertheless they were not hesitant to take advantage of the opportunities for speculation in the rates. On the other hand, the eastern part of the country, that along the Atlantic coast, had never accepted the old national paper and still retained the silver money of various Latin-American countries, especially of Peru, Chile, Guatemala, El Salvador and Honduras.[9] There was a strong prejudice here for "hard money," and the new paper córdobas were in disfavor. A considerable length of time expired before the people of the eastern coast became reconciled to the new money and were willing to adopt it as their money of account. The doubts cast upon the money by the people of these sections made the transition more difficult.

Another source of difficulty resulted from the similarity in appearance of the silver córdoba and the familiar peso or sol which had circulated throughout the entire country for so many years and which still was retained on the eastern coast. The new silver córdoba was similar in size and appearance to the old silver peso, yet the córdoba possessed a gold value more than double that of the silver peso due to the redemption privilege of the new coin. The

[9] The silver peso at this time was worth about forty-two or-three cents in American money.

people looked upon the córdoba as a peso with another name and were reluctant to accept it at a value double that of the old peso. The laborers who had been accustomed to receive fifty centavo pieces for a certain job were not willing to receive what appeared to be twenty-five centavo pieces for the same job. The people had become accustomed to have a coin of the size and appearance of the córdoba represent a certain amount of value, and were loath to accept the new coins at a value double that which they believed ought to pertain to them.

The introduction of a new currency unit necessitated a complete revision of wages and prices in Nicaragua, and this process was rendered very slow, and was accompanied by many difficulties. It was some time before prices became adjusted to the new unit, in fact there is doubt whether this adjustment is yet complete. In a backward country custom is very strong and changes take place slowly. The people of Nicaragua hesitate to quote prices at what seem to them very low values, thinking in terms of the old coins. This attitude has tended to impede the process of adjustment to the new level, with the result that prices are somewhat higher than they would otherwise be. This higher price level is apparent to the traveler upon reaching Nicaragua from neighboring countries.

The years 1912 and 1913 were bad years for Nicaragua commercially. The coffee crop for 1912 was poor, and early in 1913 there was a sharp drop in coffee prices. This fall in price caused severe losses both to the coffee growers and coffee buyers, and almost produced a crisis in business. Revolutionary disturbances also added to the difficulties of these years and to the embarrassment of the Government's finances. In spite of these difficulties the monetary reform was steadily pursued and the gold reserve built up. At the end of 1913 the Exchange Fund amounted to about 700,000 córdobas. The córdoba notes at this time amounted to about 1,571,-

000, and the total currency (notes, silver and pesos) which was exchangeabe for drafts on New York to about 2,330,000 córdobas.

Thus a sound currency system was put into operation in Nicaragua, and the Government's financial status raised in a little over a year's time, from one of insolvency to one of solvency.

5. *National Bank of Nicaragua*

THE establishment of the "Banco Nacional de Nicaragua" was provided for in the Treasury Bills Agreement of September 1911 and in the Monetary Law of March 1912. The Bank was incorporated under the laws of Connecticut in the United States, and had an authorized capital of $5,000,000. It began business in August 1912 with a paid-in capital of $100,000, which was subscribed by the Nicaraguan Government from funds provided by the New York Bankers.[10]

The Bank enjoys the exclusive right to issue notes which are full legal tender. Not even the Government is permitted to issue paper currency or any form of obligation capable of being used as money. The Bank is authorized by its charter to do a regular banking business. In addition it is the fiscal agent of the Government and depository for government funds. It also was entrusted with the transition to the new currency system and with its management once it was instituted. It was given control over the coining of money, the coinings to be in accord with the monetary arrangements, and the Bank to be given compensation for its services. The currency experts held that the coining of money was a prerogative of the state, and that the Bank in undertaking this function did so only as an agent of the state. The coining of money was considered different

[10] Article 7 of the Monetary Law instructed the Minister of Finance to subscribe on behalf of the Government to the Capital of the Bank a sum not exceeding $500,000, and to pay for this subscription out of the proceeds of the loan negotiated between the Bankers and the Government.

from the function of issuing bank notes. The two functions, however, are fundamentally the same in principle, but for practical purposes it is often well to distinguish them.

Much thought was given to the method of securing the notes and to the "currency principle" versus the "banking principle" which received so much attention in England at the time of the Peel Act of 1844. According to the currency principle paper currency should be secured dollar for dollar in cash, at least above a fixed minimum, while the banking principle argued that the paper currency was sound if secured by the general assets of the bank with a certain proportion of cash on hand or within easy call, the amount of cash to be determined by statute or conservative banking policy. Conant and Harrison believed that thirty per cent of the circulation might be entirely fiduciary, arguing that in a country where the main currency was paper the public would under no circumstances tender as much as seventy per cent of the currency for redemption at one time. They recommended that there be kept against the total circulation a gold reserve of forty per cent, and that for the remainder there be prime bills of short duration, thirty days or less; thus the total currency would be, thirty per cent fiduciary, and seventy per cent covered, with four-sevenths of the coverage in gold and three-sevenths in commercial paper. In order to provide elasticity they recommended that when the reserve had been fully built up an increase in the uncovered issue be allowed to the extent of ten per cent of the total note circulation, which excess was to bear a tax, and beyond this a further ten per cent with a higher tax.

However, these recommendations were not fully carried out. Instead of an uncovered circulation of thirty per cent, a definite amount was decided upon, about 1,600,000 córdobas. This amount was determined by the amount of funds available for buying up the old paper pesos, and was very much in excess of the thirty per

cent. All in excess of this fixed amount, however, is to be covered córdoba for córdoba in the equivalent of gold, since new notes are given out only in return for funds laid down in New York which are credited to the account of the Exchange Fund on deposit there.

Conant and Harrison recommended that the Bank be divided into two departments, the Currency Department and the Banking Department, similar to the arrangement prevailing in the Bank of England. The Bank in the administration of its affairs, and in the performance of its obligations in regard to the maintenance of the currency system has followed out these recommendations, and as a matter of practice considers itself divided into two departments, the Banking Department and the Issue Department which is run for account of the Government. This division of the Bank into two departments is merely a matter of bookkeeping. If the Banking Department, which handles the regular banking operations, needs more currency it goes to the Issue Department and presents a draft on New York and in return secures córdobas. The draft is then deposited in New York to the credit of the Exchange Fund. Thus the currency in Nicaragua is only increased as drafts on New York are sold to the Bank for córdobas and turned over by the Banking Department to the Issue Department, or as funds are presented to the agent of the Bank in New York, the Bank of Central and South America, which is charged with the custody of the Exchange Fund, and are credited by it to the Exchange Fund, a draft on the Bank of Nicaragua being given in return, which draft is paid in córdobas. Conversely the currency in Nicaragua is contracted by córdobas being presented by the Banking Department to the Issue Department in purchase of a draft on New York which draft is drawn against the Exchange Fund.

The Bank has its own deposit in New York against which it sells drafts in the ordinary course of business, and the Exchange Fund

does not come into play unless the Banking Department presents notes to the issue Department for drafts on the Fund in order to build up the Bank's own balance in New York. Other banks in Nicaragua come to the National Bank for drafts on New York when their deposits abroad become depleted. The Bank charges a slight premium for drafts against the Fund. This premium determines the "gold export point" as it would be called in gold standard countries.

Exchange rates on New York have fluctuated within narrow limits since the inauguration of the system—with the exception of a few months after the outbreak of the European war—as can be seen from the table on page 180.

The following tables show the amount of currency in circulation in Nicaragua, and the size of the Exchange Fund, at different dates.

NICARAGUA, NOTE CIRCULATION AND RESERVE FUND

1913-1923

Córdoba Notes of Banco Nacional de Nicaragua

		Circulation	Reserve Fund			
			Deposit in New York	United States Currency Awaiting Shipment	Cost of Metallic Currency	Total Reserve
1913	March	44,900				
	June	589,600				
	Dec.	1,571,00	694,368.06			694,368.06
1914	June	1,673,800	345,232.44			345,232.44
	Dec.	1,481,500	30,710.76			30,710.76
1915	June	1,521,500	21,966.37			21,966.37
	Dec.	1,648,500	13,211.66			13,211.66
1916	June	1,719,100	77,183.47			77,183.47
	Dec.	1,649,100	1,676.51			1,676.51
1917	June	1,649,100	1,693.87			1,693.87
	Dec.	1,899,100	236,872.35		121,238.91	358,111.26
1918	June	2,659,100	1,089,086.62		121,238.91	1,210,325.53
	Dec.	3,159,100	1,490,463.51		121,238.91	1,611,702.42
1919	June	4,109,100	2,421,272.97		121,238.91	2,542,511.88
	Dec.	3,739,100	2,064,439.89		121,238.91	2,185,678.80

		Circulation	Reserve Fund			
			Deposit in New York	United States Currency Awaiting Shipment	Cost of Metallic Currency	Total Reserve
1920	June	3,200,000	1,531,015.77		121,238.91	1,652,254.68
	Dec.	2,800,000	1,140,330.37		121,238.91	1,261,569.28
1921	June	2,150,000	481,176.42		121,238.91	602,415.33
	Dec.	1,860,000	185,476.84		121,238.91	306,715.75
1922	June	2,050,843	322,238.70	48,792.90	125,068.76	496,100.36
	Dec.	2,229,580	478,411.26	44,229.00	126,121.70	648,761.96
1923	June	2,571,475	787,433.88	135,562.93	126,121.70	1,049,118.51
	Dec.	2,581,609	834,198.92	149,949.43	126,121.70	1,110,270.05

Data furnished by Bank of Central and South America and by Banco Nacional de Nicaragua.

Further assistance to Nicaragua was provided by the Bankers in contracts signed October 8, 1913. The Bankers purchased another issue of treasury bills from the Government to the amount of $1,060,000 bearing interest at six per cent, the Government receiving $1,000,000. The Bankers at this time bought fifty-one percent of the stock of the National Railway from the Government, paying $1,000,000 for it. They had been actually operating the railway for over a year. The Government thus came into possession of $2,000,000 which it agreed to employ in the payment of all its obligations to the Bankers and to the National Bank. The capital of the Bank was increased from $100,000 to $300,000. Of this increase the Bankers subscribed $153,000, which thus gave them fifty-one shares of the stock, and the Government subscribed $47,000, which brought its interest in the Bank up to $147,000, or forty-nine shares. In September 1924 the Bankers sold their fifty-one shares to the Government for a consideration of $300,000. The Bank in the meantime had accumulated a considerable surplus out of earnings. Article nine of the contract of 1913 provided that of the nine directors of the Bank six were to be named by the New York Bankers, two by the Minister of Finance, and one by the

United States Secretary of State. A similar arrangement was made in regard to the railway. If the Government ever desired to sell any or all of its shares in either the Bank or the railway the Bankers were given a prior right to purchase such shares.

The contracts of October 8, 1913, also provided that $350,000 be added to the Exchange Fund. The Fund was to be kept in a special account apart from the other funds of the Bank, deposited either in London or New York, as previous dispositions had already arranged. An important provision contained in the contract was that if the Exchange Fund ever fell below $100,000, it should be replenished until it reached $200,000. The replenishment was to be affected as follows: The Bank should notify the Minister of Finance and the Collector of Customs whenever the fund fell below $100,000. The Collector of Customs, after paying for the expenses of collecting the customs revenues and after remitting to New York or Europe the sums necessary to provide for the various obligations of Nicaragua in these countries, should deposit in the Bank to the credit of the Fund, at least monthly, an amount equal to twenty-five per cent of the gross custom duties, until the Fund should reach $200,000. This lien on the customs revenues, however, has never been called into use, since the Fund was formally closed in December after the war started, and in August 1915 the provisions for replenishment were suspended.

The $350,000 which the contract provided as an addition to the Exchange Fund was to be paid by the Republic out of the funds received from the Bankers. After paying its obligations to the Bankers and to the National Bank, and after deducting the other amounts noted, the Government had to its credit of the $2,000,000, about $750,000 which was used for current expenses and various other local purposes.

In 1915 there was organized in New York the Mercantile Bank

of the Americas by Brown Brothers and Company, J. and W. Seligman and Company, and other banking interests. It became affiliated with numerous institutions throughout South and Central America, and took over the controlling interest in the National Bank of Nicaragua. It kept the Exchange Fund in New York for the Nicaraguan currency. When the price of sugar and coffee dropped in 1920 and 1921 the Mercantile Bank which was interested extensively in these commodities became involved in difficulties. Its affairs were liquidated and a new bank was organized, the Bank of Central and South America, with a capital of $5,000,000 and surplus of $2,500,000. This latter institution took over the interests of the Mercantile Bank in the National Bank of Nicaragua, and at the present time is the depository for the Exchange Fund. This new bank keeps deposited with the New York Federal Reserve Bank securities which serve as a guarantee for the Exchange Fund. These securities are held in the name of the Bank of Central and South America and are kept only at the volition of the bank. There is no legal compulsion requiring that such securities be kept. Nevertheless this procedure serves to provide a certain guarantee for the safety of the Fund. The Exchange Fund is discussed further in the following chapter.

Chapter XV

NICARAGUA UNDER THE NEW REGIME

1. *Political events*

IN the latter part of 1912 while currency reform was in progress the political situation again became disturbed, and interfered with the financial reorganization which was in process. The Minister of War under the new administration was General Mena, a prominent participant in the recent revolutionary struggle. His military successes and his popularity with the army had given him a position of influence and prestige which made him one of the dominant figures in the new Government. He was a rival of Estrada, and a signatory to the Dawson Agreements of November 1910, which endeavored, among other things, to bring about an understanding among the different leaders of the revolution. The agreements provided that Estrada be head of the new Government. A constitutional convention met in December 1910 and elected him provisional president for two years.

In spite of the Dawson Agreements strained relations continued to exist between Estrada and General Mena, and when General Mena in 1911 attempted to fill the national assembly with his personal friends by means of his control over the army, matters came to a head. The good offices of the United States Minister prevented serious fighting, and the result was that Estrada resigned and Díaz, vice-president, succeeded him in office, General Mena consenting to the arrangement and remaining Minister of War.

General Mena was left more powerful than ever, and in October 1911 had the assembly elect him president for the term which was to begin January 1, 1913. The situation was threatening, and the continual turmoil led President Díaz in December 1911 to appeal

to the United States for aid, asking that the United States intervene in the internal affairs of Nicaragua, and that relations be established between the two countries similar to those prevailing between the United States and Cuba. The following is from a letter he wrote in December 1911 to the American Chargé d'Affaires, asking that the letter be transmitted to the State Department in Washington.[1]

> "An irreconcilable division therefore separates the political parties, and the Government consequently has to maintain itself, as in a campaign, against the constant conspiring of its opponents; in short, the result may be called a state of war. It has lasted for years, and, of course, the economic consequences are profound; and this same violent politics is also the reason for the prevalence of sanguinary crimes, which can not be successfully dealt with by court and juries, since in the juries passion defeats justice almost always.
>
> "On these two problems I have seriously meditated and disconsolately conclude that lasting and stable peace, order, economy, moderation, and liberty can not come through our own means; and that the grave evils affecting us can be destroyed only by means of more direct and efficient assistance from the United States, like that which resulted so well in Cuba.
>
> "It is therefore my intention by means of a treaty with the American Government to so amend or add to the Constitution as to assure that assistance, permitting the United States to intervene in our internal affairs in order to maintain peace and the existence of a lawful government, thus giving the people a guarantee of proper administration.
>
> "Before opening official negotiations I wish to learn privately through you the opinion of the Department of State, and if you can do me this favor you will also render thereby a great service to this country.
>
> Adolfo Díaz."

The State Department replied to President Díaz saying that

[1] *Foreign Relations of the United States*, 1911, p. 670.

careful consideration would have to be given the request before an answer could be made.

In the meanwhile opposition to General Mena had been pronounced but no outbreak had occurred. About the middle of 1912 President Díaz felt that he was in a stronger position and attempted to remove Mena from office as Minister of War. Mena then fled from the capital with a large part of the army and secured possession of most of the Government's ammunition and supplies. Other factions joined him and in a short time open hostilities had begun. General Mena made repeated assurances, which he had no intention of keeping, as later developments proved, to the American Minister, Mr. Weitzel, who was endeavoring to hold matters in check. Mr. Weitzel, confident of his ability to cope with the situation, discouraged President Díaz and the Government from making active preparations to suppress the revolution. The revolution rapidly gained momentum and the friends of the deposed Zelaya allied themselves with Mena. The Government was weakened by the loss of most of its army and ammunition, which was in the possession of Mena, so that success by Mena and the Zelaya group appeared likely.

This was the condition of affairs in August 1912. President Díaz was in a precarious position with the rebel forces closing in on him from all sides. The American Minister was receiving complaints from various sources of depredations by the revolutionists. The American colony, and various other individuals, urged upon the Minister the necessity of taking prompt action to assure protection to lives and property. The Minister thereupon asked the Government of Nicaragua to guarantee protection to the foreigners in the country. This Nicaragua could not do. The Minister of Foreign Affairs replied to the demands of the United States that his Government was making every effort to extend such protection, but

regretted its inability to do so. In conclusion he said: "My Government desires that the Government of the United States guarantee with its forces security for the property of American citizens in Nicaragua and that it extend its protection to all the inhabitants of the Republic."[2]

After events of the preceding years, and with conditions in Nicaragua as they were, the American Government could not remain aloof and permit the Zelaya group to overthrow the Government and inaugurate its old régime, a régime notorious for oppression and petty despotism, and one which had been condemned by all the Central American countries as well as by the countries of the world. If Zelaya's men were returned to power the efforts of the United States to rehabilitate Nicaragua economically and politically, and to assure her people a respectable government, would have been vitiated. Currency reform was already under way and loans by the New York Bankers had been extended providing Nicaragua with funds. The American Government had become tacitly committed to a policy of restoration of order, and economic rehabilitation of the country.

The American Minister sent a telegram on August 3, 1912, to the commanding officer of the U. S. S. *Annapolis* which was off Corinto asking that he disembark a guard and send it to the Legation in Managua. In response to this one hundred men were landed and reached Managua in the early morning of August 4. A bombardment of Managua by the rebels took place beginning August eleventh and lasting until the morning of the fourteenth. The small American force was insufficient to cope with the situation, and a larger force which had been dispatched from the Canal Zone was enroute, but had not yet arrived in Nicaragua. In the meantime

[2] *Foreign Relations of the United States*, 1912, p. 1032.

the Minister of Foreign Affairs sent a note to the American Minister, Mr. Weitzel, asking that more American troops be landed. On the morning of the fourteenth, shortly after the bombardment had ceased, 350 American troops from the Canal Zone arrived in Managua, much to the relief of the inhabitants, and the situation in the city became quiet.

The railway which ran from Corinto, the port on the Pacific side, to Managua, the capital, and points beyond, was interrupted by the rebel forces. The railway at this time was owned by the Nicaraguan Government and was operated by the Bankers as part of the agreement whereby loans were extended. American marines took over the railway, and in a short time traffic was resumed over the entire length of the line although the revolutionists held all the important cities through which the railway passed, with the exception of the capital.

The revolutionists were reluctant to submit and several engagements with American forces took place before order was restored. Under date of September 4 the State Department sent a message to Minister Weitzel with instructions to transmit it to the Nicaraguan Government, and to communicate it unofficially to the rebel leaders, and to make it public, as the declared policy of the United States. The message in part was as follows: "The policy of the Government of the United States in the present Nicaraguan disturbances is to take the necessary measures for an adequate legation guard at Managua, to keep open communications, and to protect American life and property.

"In discountenancing Zelaya, whose régime of barbarity and corruption was ended by the Nicaraguan nation after a bloody war, the Government of the United States opposed not only the indi-

vidual but the system, and this Government could not countenance any movement to restore the same destructive régime."[3]

This positive statement on the part of the United States disheartened the revolutionists and General Mena surrendered to Admiral Southerland at Granada on September 25. Shortly afterwards the other leaders were forced to submit. Eight American naval vessels participated in the campaign, with 125 officers and 2,600 men, seven of whom lost their lives.[4]

Most of the United States troops were withdrawn immediately after the revolution was suppressed, but since this time about 100 marines have been stationed at Managua. The withdrawal was begun in October 1912 and by the end of the year all were gone except a legation guard of 400. This was later reduced in size to 100.

The continued presence of these marines has served to keep things quiet so that there have been no serious outbreaks against the Government, although disturbances have occurred from time to time. This support has kept the present administration in power, and were the marines withdrawn the Government would perhaps soon be overthrown by its opponents. Elections are held from time to time, but in a country like Nicaragua it is well nigh impossible to have an election that is really representative and little more than a formality. The present administration in Nicaragua is unpopular although it has given Nicaragua better government than she has experienced before.

2. *Operations of the currency system*

The new currency system began its existence under difficult circumstances. The Mena revolution and political disturbances took

[3] *Foreign Relations of the United States*, 1912, p. 1043.
[4] *Report of United States Secretary of the Navy*, 1913.

place when the system was still in process of installation. Then in the middle of 1914 when it was starting on its second year came the war in Europe. The war found Nicaragua in the midst of a business depression with the economic condition of the country unsatisfactory. The crops had been damaged by pests and unfavorable growing conditions so that the agricultural class was not prosperous. The financial troubles of the Government were great. The suppression of the Mena revolution had entailed considerable expense upon the treasury already struggling to become solvent, and the continual turmoil and political agitation had interfered with the Government's ordinary revenues. Foreign credits to local merchants were overstrained due partly to the optimism regarding the prosperity which was expected to follow the financial rehabilitation of the country. Hopes of receiving $3,000,000 for the sale of canal rights according to the treaty with the United States were not yet fulfilled.

Trade with Germany was almost completely cut off by the war, and that with other European countries was greatly affected. Nicaragua normally shipped the bulk of her coffee to France and when this market was suddenly cut off the coffee growers were placed in an embarrassing position. Credits extended to Nicaraguan merchants and coffee exporters were suspended or greatly curtailed, and the whole situation was so involved that a general moratorium was declared by a law of October 23, 1914.

As credits abroad were called in the demand in Nicaragua for drafts placed an abnormal strain upon the Exchange Fund. The drain upon the Fund led the National Bank in October 1914 to suspend entirely the sale of bills of exchange, although this was contrary to the provisions of the monetary law. As soon as the Bank ceased selling drafts the rate of exchange began to rise, and the premium on dollars at its maximum amounted to about thirty

per cent. On December 2 a contract was negotiated between the Bank and the Government by which the Bank was relieved from its obligation of redeeming córdobas in drafts; thus the aspect of illegality was done away with.

European credits to the local merchants and coffee growers were withdrawn as soon as the war began, as noted above, so recourse had to be had to the local banks to help finance business ordinarily financed abroad. The coffee growers were especially desirous of funds to move their crops which were then ready for moving. This demand for relief and for more money found expression in the above mentioned contract of December 2, 1914. The Bank was authorized by this agreement to issue additional córdobas to the extent of 1,500,000. Accordingly the Bank issued 500,000 córdobas which went to the Government to meet its obligations, many of which were overdue. The new notes were to be retired as promptly as possible, and to assist in amortizing them, the proceeds of a property tax, established in the latter part of November and to be collected by the Bank, were to be applied to the retirement of this emergency issue.

An outstanding fact about this contract of December 1914 was that it closed the Reserve Fund in New York to the sale of drafts as long as any of this emergency issue of currency should remain outstanding. One of the fundamental principles of the gold-exchange standard is that if the currency becomes redundant and thus depreciated in terms of gold, contraction is automatically brought about by the notes being presented for redemption in drafts payable in gold. The tendency of the new issue of notes was to depreciate the currency and raise exchange rates on gold standard countries. This would cause a further drain upon the Exchange Fund; consequently to prevent this contingency and to avoid the necessity of a possible replenishment of the Fund from

customs revenues, which would weaken the credit of the Government, there was inserted in the contract the provision that the Fund be closed as long as these emergency notes remained in circulation. The amount of inflation due to this additional issue of notes—which served as a basis for credit in Nicaragua—can not be accurately determined since the new credits were taking the place in large measure of foreign credits withdrawn. In fact the purpose of the new issue was to fill up the void left by the withdrawal of foreign credits, and if this were all that were done there would have been no basis for closing the Fund on this score.

The practical expediency, however, of closing the Fund on account of the general financial crisis, has something to be said in its favor, but it is to be recognized as an abandonment of the gold standard. The purpose of maintaining a large reserve fund is to be able to meet emergencies, and if when the emergency arises the Fund is made unavailable and not utilized to the limit, its full usefulness is not realized and the part not used might as well not have been kept at all. On the other hand if there is real danger of complete annihilation of the Fund, by closing the Fund before it reaches zero there is something retained with which to start over again when the emergency shall have passed. The Fund when it was closed in December 1914 had been reduced to only $33,591 from about $350,000 a few months previously, and from about $700,000 a year previously. Thus the necessity of closing the Fund is apparent.

As soon as the National Bank, in the fall of 1914, discontinued selling drafts for córdobas in accordance with the monetary law of March 1912 the price of drafts rose. They continued rising in price and in a few months a premium of twenty-five or thirty per cent prevailed, 125 or 130 córdobas were required to purchase $100 on New York. The National Bank was not allowed to sell drafts

at much above par according to the monetary law, so it withdrew from the market, and drafts were sold by the other banks and dealers.[5] The National Bank made arrangements with the Commercial Bank of Spanish America for the selling of drafts, and through the operations of the latter bank the premium on bills of exchange was reduced in a few months time. Around the beginning of 1916 the National Bank resumed the sale of drafts, charging only the customary premium as allowed by law.

It will be remembered that according to the contracts of October 1913 whenever the Exchange Fund in New York fell below $100.-000 the Collector of Customs was required to turn over a certain portion of the custom receipts each month until the fund amounted to $200,000. A presidential *acuerdo* of August 23, 1915, declared that this provision of the contract be suspended until July 1, 1916. A plan was worked out in 1917 reorganizing the country's finances and the relations between the Bankers and the Government, and was adopted in November 1917. This Financial Plan of 1917, as it was known, provided in Article Two, Section Four, that as soon as the Exchange Fund should be reopened (closed under the contract of December 1914), the provisions for replenishing the Fund from customs revenues in accord with the contract of October 1913, should again be in force. Similar provisions regarding the suspension of the arrangements for the replenishing of the Fund were embodied in the Financial Plan of 1920 which replaced that of 1917.

The Financial Plan of 1920 contained an important provision regarding the closing of the Exchange Fund. Among other things

[5] In addition to the National Bank there exist in Nicaragua the Anglo Central American Commercial Bank, Ltd., also the Commercial Bank of Spanish America, Ltd.

the Plan provided for the issuance from time to time by the Government of Nicaragua of interest bearing Treasury Bills in denominations of not less than $1,000, such Treasury Bills, to fall due on the first of February or the first of August following the date of their issue. The Government might issue a new lot of Bills to pay off those maturing, but in no case were there to be any outstanding after the first of August 1924. The contract of December 1914 had provided that the Exchange Fund be closed as long as any of the emergency issue of currency remain outstanding. This emergency issue has been largely retired and in January 1923 only about seven thousand córdobas were still outstanding. The Financial Plan of 1920 provided, Article Two, Section Four, that the Exchange Fund should remain closed as long as any of the Treasury Bills continued outstanding. The last of the Treasury Bills were paid off by August 1, 1924, as arranged in the Financial Plan of 1920 so that the provision in the Plan regarding the closing of the Exchange Fund is no longer effective. The small amount of the emergency currency still out might easily be called in or outlawed after a certain date, and the Fund would then automatically be opened and the provisions for replenishment once more be in force. The Fund is now in fairly good shape as can be seen from the table on pages 165-166, and amounts to about forty per cent of the circulation.

Although the Exchange Fund has been formally closed since December 1914 and the Bank has not been required during this time to redeem córdobas in drafts, the Bank has in fact made a practice of selling drafts for córdobas. Thus the benefits of the gold standard have been enjoyed. It charges at present a premium of two per cent for drafts on New York, as can be seen from the table on the next page.

Exchange Rates on New York in Nicaragua
Selling rates for sight drafts by Banco Nacional
Córdobas for 100 dollars

1912	December	101	1919	June	101.50
1913	June	101		December	101.50
	December	101	1920	June	101.50
1914	June	101		December (rose to 102 July 28)	102
	December		1921	June	102
1915	June	112.5[1]		December	102
	December	105.5[1]	1922	June	102
1916	June	101		December	102
	December	101	1923	June	101.5
1917	June	101		December	101.5
	December	101			
1918	June (rose to 102 June 22)	102			
	December (declined to 101.50 Dec. 3)	101.50			

The Financial Plan of 1917 established what is known as the High Commission (Alta Comisión). The Commission consists of three members, one appointed by the President of Nicaragua and to be a citizen of Nicaragua, another appointed by the Secretary of State of the United States and to be a citizen of the United States, and a third to act as umpire in case of disagreement between the other two, and who shall be appointed by the Secretary of State of the United States, to be a citizen of the United States. The purpose of the High Commission is to assist Nicaragua in the conduct of her finances and to see that the conventions entered into are carefully carried out. The Commission acts as arbitrator over certain questions that arise and has various other duties. If the Government needs more revenue than that allowed it each month according to the budget, it must secure the consent of the High Commission. The Commission thus serves as a safeguard for the Guaranteed

[1] Average selling rate Anglo Central American Commercial Bank, Ltd.

Customs Bonds which were issued to liquidate and consolidate the debt of the country. The American members of the Commission are Roscoe R. Hill, who resides in Nicaragua, and Professor J. W. Jenks, who serves as umpire.

The consolidation of the country's indebtedness by the Financial Plan of 1917 was aided by the receipt of $3,000,000 from the United States Government under the terms of the Canal Treaty ratified by the United States Senate in February 1916. When the loan treaty signed in June 1911 failed of ratification in the United States Senate, a new treaty was drawn up which provided that Nicaragua grant to the United States the right to establish a naval base in the Bay of Fonseca, on the Pacific side of Nicaragua, and that it also grant to the United States exclusive rights to build a canal through Nicaragua from the Atlantic to the Pacific by way of Lake Nicaragua and the San Juan River. For these privileges the United States was to pay Nicaragua the sum of $3,000,000. This treaty, known as the Bryan-Chamorro treaty, was signed on August 5, 1914 but met with considerable opposition in the United States Senate. It was opposed strongly by the other Central American States, and Latin-American countries, and was considered by them as evidence of American aggression south of the Rio Grande. It was finally ratified by the United States early in February 1916 and the money was later made available for Nicaragua's use.

Part of the money received from the United States in view of the Canal Treaty was used by Nicaragua to pay off various debts and claims against the Government as determined by the Commission on Public Credit. This Commission was established by a law of February 14, 1917, and was to examine the claims of all creditors against the Government, except those by virtue of funded debts, and was to make awards for their payment partly in cash made available by the Canal Treaty and partly in bonds to be issued by

Nicaragua, arranged for in the Financial Plan adopted later that year. The Commission was composed of three members, two nominated by the Department of State of the United States, and one chosen by the President of Nicaragua. The American members were Mr. Abram F. Lindberg and Professor Jeremiah W. Jenks, and the Nicaraguan member was the Minister of Finance, Señor Don Octaviano César.

The Commission made a careful study of all the claims presented against the Government, about 3,800, and in the latter part of 1917 declared its awards. There were some delays before the money was available for payments, but in May 1918 the payments began and as the claimants received their money the documents supporting their claims were turned over to Nicaragua with final receipts.

3. *Summary*

At the present time Nicaragua is not legally upon the gold-exchange standard, and except for a period of a little over a year in 1913 and 1914 never has been. The provisions for selling drafts have been in suspense since the Exchange Fund was closed in December 1914, and the provisions for replenishing the Fund from customs revenues have been in suspense since August 1915. However, through the operations of the National Bank, the country has enjoyed the benefits of the gold standard, and had stable exchange rates when practically all the other countries of the world were experiencing erratic fluctuations. For a few months during the early part of the war exchange rates were allowed to rise, but they were soon brought back approximately to par and have been maintained thereabouts ever since.

The depression of 1920 brought a strain upon the currency system and there were rumors that the Bank would exercize its option

and refuse to redeem córdobas in drafts on New York. This the Bank did not do, but maintained exchange rates at close to par although this involved considerable expense to itself.

A certain amount of American money circulated in the country and this was shipped out to build up deposits in New York against which drafts might be drawn. Interest rates in Nicaragua were especially high, and in some cases were as much as twenty-five or thirty per cent. The rate of the National bank is twelve per cent, and when loans were made this rate was adhered to, although the Bank could have charged more.

The Bank has been the subject of much criticism in Nicaragua and has been described as an institution to exploit the country. The bulk of the criticism seems to be founded upon prejudice, lack of information, and misinformation. Whatever unfortunate events may have taken place, are of the kind which are apt to take place with most any institution. Professor J. W. Jenks visited Nicaragua as an Inspector of the Bank in 1918 and again in 1922, and reports favorably on the condition of the Bank and on its operations. He describes it as thoroughly sound and as co-operating with the people of Nicaragua. The Bank has established branches in several of the more important cities and towns, and in this way is extending its facilities to the different sections of the country.

An institution was established in Nicaragua, owned by the Mercantile Bank of the Americas, known as the Ultramar, or Overseas Corporation. This was an importing and exporting house and dealt in coffee, sugar, and general merchandise. The Ultramar was in a position to purchase to advantage in the United States and to offer effective competition to the local merchants. The Ultramar was not distinguished from the Bank by the Nicaraguans, and it was charged that the Bank was going into business and competing with its own customers. The Ultramar tended to aggravate the an-

tagonism towards the Bank and was exceedingly unpopular. It had large dealings in coffee and in sugar, and when the prices of these commodities fell precipitously in 1920 and 1921, the institution became involved and lost heavily. It was later liquidated. Since the Ultramar was distinct in organization from the National Bank, although owned and controlled by the same group—the stockholders of the Mercantile Bank of the Americas—the National Bank was spared heavy losses which otherwise would doubtless have fallen upon it.

Business conditions in Nicaragua, due to the depression of 1920 and to the fall in the prices of coffee and sugar, were bad. Coffee growers were in need of funds and many merchants and importing houses were embarrassed in making remittances abroad. The depressed conditions were reflected in the finances of the Government which was struggling to meet its obligations. The foreign trade declined in 1921 from the high point of the previous year, as can be seen from the following.

	IMPORTS	EXPORTS
1920	13,864,390	10,787,330
1921	5,309,900	8,070,950
1922	5,123,500	7,903,450
1923	7,268,400	11,028,310

Soon after the opening of the war in Europe the Government was forced to suspend the service of its sterling loan due to the falling off of customs receipts. Satisfactory arrangements for this suspension were made with the Corporation of Foreign Bondholders. Nicaragua, however, experienced difficulty in keeping up her payments since conditions were slow to improve. Almost continually since foreign financial control was inaugurated in 1911, conditions in Nicaragua have been disturbed, first by local revolu-

tion, then by the war in Europe, and finally by a severe business depression which caused a marked decline in Government revenues. Conditions since this time have been improving and Nicaragua is now in a more healthy and prosperous state.

The total debt of Nicaragua on March 31, 1924 was as follows:

Bonds of 1909 Outstanding £864,760[6]........	C $4,208,159.88
Guaranteed Customs Bonds................	3,250,900.00
Bonds of 1904...........................	30,000.00
Treasury Bills of 1920....................	300,000.00
Debts and Claims........................	350,000.00
	C $8,139,059.88

This figure of 8,139,059 córdobas for the total debt at the end of March 1924 is in contrast to that of about 32,200,000 for the debt on January 1, 1912, and to that of 22,100,000 for the debt on November 1, 1917, prior to the Financial Plan of 1917. These reductions were brought about by paying off some of the debts and by refunding and reducing others through settlement.

The relations between the United States and Nicaragua, in which the Bankers have played a prominent part, have been the subject of much bitter discussion and criticism throughout the United States, and throughout all Latin-American countries. From the economic standpoint the system has been a success. The years of financial control have been ones of special turmoil throughout the world in general, and affairs in Nicaragua have been carried on under difficulties. Nevertheless the economic condition of the country is fundamentally sound, and business is carried on with confidence. Progress has been made in several ways, such as reform and stabilization of the currency, and improved service over the railroads. The payment of government salaries has not been al-

[6] Converted to córdobas at rate of 4.8665.

lowed to remain continually in arrears. In the matter of education and sanitation there is still much to be desired. Education is not compulsory and large sections of the country have no public schools whatsoever.

Politically the system is successful in that it has given the people a stable government, and one that does not reek with favoritism and oppression as did the Government of Zelaya. The present Government is not entirely free from the evils of favoritism and corruption, but to eliminate them still more control would have to be taken out of native hands, and it is to be remembered that even our own governments are not free from these evils. The American administrative officers in Nicaragua have manifested special efficiency and integrity, and have performed their duties well. Under the American control the agricultural population in Nicaragua have been free to follow their pursuits without interference from revolutionists carrying off their cattle and other property; for this they are grateful to the United States.

The Bankers have acquitted themselves satisfactorily in Nicaragua and what mistakes have taken place have been largely those of lack of tact and of misunderstanding of native ways. By greater publicity on the part of the Bankers much needless antagonism would have been avoided. The Bank seldom gives out statements of its condition, or data on the condition of the Exchange Fund. However, there seems to be no lack of confidence in the Bank's currency, and the people prefer the paper notes, even the smaller denominations, to silver money, of which the bank has a large supply in its vaults and which it finds difficult to force into circulation.

The collectorship of the customs is perhaps the most conspicuous part of the American relations with Nicaragua, and from both the standpoint of efficiency and freedom from corruption, which unfortunately permeates nearly all Latin-American administrative

offices, is preëminently successful. The service has been reorganized and put upon a businesslike basis so that the revenues received by the Government have increased.

The antagonism toward the United States and toward the American Bankers is due in large part to agitation by political malcontents who see no possibility of acquiring power and opportunities for personal enrichment as long as the United States holds on the lid. Nevertheless, it is desirable in several ways that the United States restore eventually to Nicaragua more control over her affairs than she now has. A withdrawal of the marines will improve relations with all Latin-American countries; and under proper arrangements such a withdrawal might be consummated in the not very distant future. In the event of misgovernment or disturbance, a firm hand by the United States might again become essential. The United States Government has recently announced that plans are being formulated for the withdrawal of the marines.

The collection of the customs involves a different problem, and the present arrangements must be maintained as long as the outstanding obligations are unpaid. Where domestic conditions warrant, an arrangement such as prevails in Costa Rica is less offensive to national ambitions and sentiments, and also provides security for the borrowing of needed capital. If Costa Rica defaults in the interest payments on her foreign debt a collectorship of the customs is automatically established, giving the agent of the loan, Mr. John M. Keith, the right to collect all the customs duties through the issuance of certificates, the customs duties to be payable only in such certificates.

One of the reasons that economic improvement in Nicaragua is not more evident than it is, is because a considerable portion of her revenue is now going to pay off debts which formerly were in default and thus were no drain on her finances. This revenue was

formerly going largely to government officials and their friends in Nicaragua, and to maintain the army. It is now used to restore the country's credit and to provide internal improvements. As the revenue increases and the foreign debt diminishes more money will be available for internal improvements. The return which she now gets for the money spent on the foreign debt service, a return more or less concealed, is renewed credit in the markets of the world. Among the most apparent and important benefits which Nicaragua receives from the new administration are a relatively stable currency system, together with non-fluctuating exchange rates.

PART V COSTA RICA

Chapter XVI

MONETARY HISTORY PRIOR TO 1914

1. *Spanish system of currency retained after independence in* 1821

AFTER Costa Rica secured its independence from Spain in 1821 it retained the Spanish system of currency with which the country was familiar. The gold coin was the "onza de oro," or "doubloon" as it was called, equal in value to sixteen of the silver pesos. Agitation was soon commenced for the establishment of a mint for the coining of money in Costa Rica and in 1824 the establishment of the "Casa de Rescates" was ordered. Operations were finally started in 1828, with three employees sufficing for the work. Although a considerable amount of national money was put into circulation, Spanish and other foreign coins remained the chief circulating medium.

This mixed condition of the currency continued down to the end of the nineteenth century and was the source of much confusion. Disparity in the weights and finenesses of the coins of the different countries, especially the coins from South America, constituted a disturbing element in the currency and the Government frequently found it necessary to post a table rating the values of the various foreign coins, and to prohibit altogether the circulation of certain debased coins such as some of the Honduran "silver" which was actually fifty per cent or more copper, or some of the Peruvian coins which also contained a large amount of copper.

Money of irregular shape, odd pieces of silver cut to the proper weight and containing the official stamp, so-called "moneda macuquina," or "macacas," circulated in Costa Rica as in other countries of Central America, and being comparatively easy to counterfeit was frequently counterfeited. This fact brought all the "moneda

macuquina" under suspicion whether legitimate or not. As a result the Government determined to withdraw it from circulation and ordered it brought to the mint and exchanged for money of regular shape and design. Finally, in July 1849, its circulation was prohibited altogether, a step Guatemala did not take until 1873.

The decimal system was introduced into the currency by Costa Rica in November 1863, when the peso, instead of being divided into eight reales, was considered as divided into one hundred centavos. The fifty and twenty-five centavo pieces would thus be equal to one-half and one-quarter pesos, and the equivalent of four and two reales, respectively. The gold onzas and half-onzas, valued at sixteen and eight pesos, respectively, were replaced by coins worth ten and five pesos, and thus the currency was put completely onto the decimal system.

The currency was always in a state of more or less confusion, the large amount of miscellaneous foreign coins of different metallic content being a continual source of trouble. Also, the effort to maintain bimetallism necessitated adjustments in the values of the coins with accompanying disarrangements. The gold onza originally valued at sixteen pesos in silver money, was declared in December 1841 to have a value of eighteen pesos. The following year a revolution headed by Francisco Morazán overthrew the Government and the above decree was repealed. However, in March of the following year, 1842, the gold coins were again raised in value, but this time only to seventeen pesos, a value which the South American countries were accepting. Later, in 1863, its value was raised to seventeen and one-half pesos.

The statute books of Costa Rica abound with laws and regulations relating to currency matters, mostly minor matters and necessitated by the polyglot nature of the coinage. One of the more important laws was that passed in April 1871 establishing as the

monetary unit a gold peso, worth, according to its metallic content, a trifle less than the American dollar, and having a ratio of approximately fifteen and one-half to one with the silver pesos which enjoyed customary circulation.[1]

It is to be noted that this change in the coinage was not an actual establishment of the gold standard, due to the large amount of silver coins in circulation whose metallic ratio to the gold coins was in close harmony with the market ratio of the values of the two metals. The law was in fact a readjustment in the bimetallic standard, although nominally it appeared to create the gold standard.

2. *Fall in price of silver after* 1871 *causes export of gold and leaves country with silver standard*

According to the market price of silver, the ratio between gold and silver in 1871 was fluctuating around fifteen and one-half to one, thus being in fair harmony with the monetary ratio of Costa Rica. But a year or so later the great fall in the price of silver throughout the world began, and as the gold money came to be undervalued in terms of cheaper silver, it passed at a premium and later disappeared from circulation altogether, leaving the country with the silver money. Gold coin was exported or hoarded so that by the middle of the eighties there was little of this money in circulation and Costa Rica had in fact the silver standard. When the country thus went onto the silver standard, the value of the peso in

[1] The gold peso was given a weight of 1.612 grams .900 fine. Most of the silver pesos circulating throughout Central America were 25 grams .900 fine, although together with these were ones of lighter weight, also some of heavier weight, such as those of Mexico. The largest national silver coin provided for by the new law was the fifty centavo piece. While it weighed 12½ grams, or half that of the peso in circulation, its fineness was only .835 which gives a bimetallic ratio of a trifle under fourteen and one half to one. Thus these silver coins were fiduciary.

foreign markets declined along with the fall in the price of silver, or in other words exchange rates on gold standard countries rose in Costa Rica. In the years prior to 1880 when gold money was in circulation, the premium on sterling bills was fluctuating between eight and fifteen per cent. By 1886 the premium had risen to about forty-two per cent and continued rising, averaging slightly less than 150 per cent for the year 1894. The rising exchange rates were merely following the fall in the price of silver.

3. *Currency conditions unsatisfactory*

Costa Rica had experience with paper money dating back to the early days of the country's independence. In 1839 paper money to the amount of twenty-five thousand pesos was ordered put into circulation in denominations of one, five and ten pesos to help provide for the public debt. Various issues were put out by the Government, and the issues appear always to have been made in moderation. These issues were of government paper money, and it was not until the last half of the century that bank notes made their appearance, and it was during the last quarter of the century that they became an important part of the country's currency. In 1884 a monopoly of note issue was given to the Banco de la Unión,[2] allowing it to issue notes guaranteed by a reserve of twenty-five per cent in either gold or silver. The notes of this bank came to have wide circulation throughout the republic, and together with a certain amount of government paper, issued in 1882 when poor coffee crops brought distress to the Treasury, passed currently with the silver money. Later they began to drive some of the silver from circulation and the currency came to be in large part paper. The paper money was held responsible for the exodus of gold coin, and

[2] The name of the bank was changed in 1891 to Banco de Costa Rica, under which name the bank still exists.

for the rise in exchange rates, results which were due in the main to the fall in the price of silver as already described. Dissatisfaction with the bank notes came to be one of the causes which later led to agitation for monetary reform.

Another source of difficulty was the miscellaneous character of the metallic currency. The currency still consisted of a heterogeneous mixture of foreign silver coins of different weights, especially the fractional coins. The coins were chiefly from Latin-American countries and enjoyed both customary and legal circulation.[3]

4. *Gold Standard adopted by Reform of* 1896

THE situation which induced the administration to undertake a comprehensive reform of the monetary system which resulted in the law of 1896 and subsequent measures, was the precipitous fall in the price of silver during the years 1892, 1893 and 1894, and the accompanying great rise in the foreign exchange rates, with the consequent disorders to business. The price of silver had been falling continually since about 1872, and the unhappy experiences the country was subjected to under the silver standard produced a sentiment for monetary reform, and for the gold standard. Accordingly a law was passed in October 1896 looking toward the gold standard, and adopting as the basis of the monetary system a unit, the "colón," to be worth a trifle less than fifty cents of American money, 46½ cents.[4] The smallest gold coin authorized was the piece of two "colones."

[3] In the three years 1887-1889, over 900,000 pesos in silver coin were imported into Costa Rica from various Spanish-American countries. In 1883 the Peruvian peso was made legal tender for government receipts and payments, and in 1885 and 1889 the silver of Mexico, Chile, Spain, Peru, Honduras, Guatemala, Colombia and Ecuador was given legal circulation generally.

[4] The colón contained 778 milligrams of gold .900 fine and thus was worth $0.4653 in American money.

The "colón" was divided into one hundred "céntimos" instead of "centavos." Since this time the words "colón" and "céntimo" have been used in Costa Rica, in place of the words "peso" and "centavo," but they have not succeeded in replacing completely the old familiar words, which are still heard and are used synonymously with the newer words. The subsidiary silver money provided for by the law was to be fiduciary in character, the value of the silver in the coins being less than their money value.[5]

The gold value of the new monetary unit was a little less than one-half that of the previous gold peso established in 1871. However, the peso which the country was accustomed to in 1896 was worth less than one-half the peso of 1871, as measured by foreign exchange rates. The peso of commerce and of the market place had become the silver peso, and its value as expressed in rates on London had been fluctuating during the few years preceding the monetary reform at between forty and fifty per cent of its original value. The most precipitous fall in the gold value of the peso occurred after the year 1891, and it is probable that when the reform was adopted in 1896 the country had not yet fully adjusted its wages and prices to the lower level. Consequently when the peso was stabilized at a value a little above its current gold value as reflected in exchange rates, it is probable that the new value was not far out of harmony with the prevailing level of prices and wages.

[5] The subsidiary silver coins were to be similar to those already in circulation with the change that the new coins be reduced in fineness to .750; those in circulation were mostly .835 or .900 fine. This arrangement was changed in 1900 so that all silver should have a fineness of .900. The largest silver coin provided for, the fifty céntimo piece, was given a weight of 10 grams, which at the prevailing price of silver would be worth something less than one-half a colón, the nominal value of the coin in gold.

5. Installing the gold standard

THE monetary law of October 1896 was adopted pursuant to a contract negotiated between the Government and the Banco de Costa Rica in July of the same year and which contained the details of the plan of reform. The bank had enjoyed a monopoly of note issue since 1884 and at the time of the reform had an issue of about five million pesos. By this contract of 1896 the bank relinquished its exclusive privilege of note issue, although it was favored in the matter of reserve to be maintained. The Government estimated that to establish successfully the gold standard it would need about four million gold colones. The coinage of these colones was to be spread over a period of years; five hundred thousand were to be coined immediately, and other amounts at various intervals, the whole amount to be coined by 1902. As a matter of fact the coinings were actually completed by 1900. The contract with the bank provided that the Government would deposit the new gold colones, which were to be minted, in the bank and that the bank would retire its own notes to an amount equal to ninety per cent of the gold coins deposited according to the schedule for coinings. When the Government deposited gold it was to issue gold certificates against the coin, which certificates were to be redeemable in the new colones at a date not later than December 31, 1900. This arrangement whereby the Government issued certificates to be redeemed later in gold, assisted in financing the reform. The bank, in the meantime, was to redeem the certificates in silver money and they were to be treated the same as the bank's own notes. The Government might declare the certificates redeemable in gold at any time whenever the gold accumulated amounted to 2,500,000 colones.

Arrangements were made with the United States mint in Philadelphia to coin the new colones, and as the coins arrived in Costa Rica they were deposited in the Banco de Costa Rica according to contract and gold certificates issued against them by the Govern-

ment. The bank retired its notes according to the agreement, so that there was little change in the total amount of circulating medium. To assist in financing the reform a loan of 150,000 pounds was negotiated with the banking house of Baring Brothers in London by President Yglesias when he was in England in 1899.

In April 1900 the President issued a decree that the Government had complied with its part of the contract, and that after July 15, 1900, which was six months before the date required by the law, the certificates were to be presented at the bank for redemption in gold; and that all obligations contracted in national money should be settled after that date on the basis of one gold colón for each silver peso. The national silver money was to continue circulating on this basis, but under the new law silver money was to be legal tender only to the amount of ten colones; this was later raised in 1902 to fifty colones.

On July 16, 1900, the bank began redeeming the certificates in gold, and Costa Rica was on the gold standard. About 4,000,000 colones in gold had been received from the mint in Philadelphia at this date and in the few months following the total was raised to nearly 5,000,000. Gold began to circulate freely and there was general satisfaction over the successful conclusion of the reform.

The course of exchange rates on London during the months preceding the redemption date shows how the consummation of the reform was anticipated, and the rates discounted as the time for redemption approached. A pound sterling was worth approximately 10.45 of the new colones according to gold content. In January 1900 there were needed 12.70 colones to purchase a pound. The average for May was 11.17 colones. The rates continued to fall as the redemption date approached. Specie payments were begun in July and the rate for August, when redemption was in progress, averaged 10.65 colones; par was 10.45. During the rest of the year the rates fluctuated between 10.60 and 10.70 to the pound.

With the inauguration of the gold standard Costa Rica entered upon a period of relatively stable exchange rates, and fluctuations were confined within narrow limits.

6. *Additional measures*

It will be remembered that Costa Rica had various foreign coins circulating side by side with her national money, many of them of inferior weight and fineness. One of the first moves toward monetary reform was a decree in July 1896 suspending all coinage of national silver money until a new currency system should be established.

As for the foreign silver, a period of thirty days was allowed during which time the foreign coins were to be presented at the Treasury in exchange for national money. After this date the foreign silver was no longer to be legal tender. Costa Rica thus took definite steps to rid herself of the miscellaneous foreign silver coins which had existed in her currency since the beginning of the country's history, and to establish what may be considered a truly national currency. As for gold coins, there had always been a certain amount of foreign gold coin in Costa Rica and the monetary law provided that it be legal tender and that the President determine the relation of its value to the colón. This the President did in May 1900 when he decreed that gold of the United States, England, France and Germany should be legal tender and circulate on an equal basis with the colón at specified ratios.[6] It was believed that this would give greater security to the gold standard.

[6] The ratios were readjusted in February, 1902, and were then as follows:

American dollar	2.15	colones
Pound sterling	10.45	"
Twenty-franc piece	8.25	"
Twenty-mark piece	10.20	"

These ratios were a close approximation to the actual gold par between the currencies.

The regulations regarding foreign coins were completed when a decree in August 1900 declared that the importation of all silver coins, both national and foreign, was prohibited, but that the importation and exportation of all gold coins was free and untaxed. This latter provision, unhampered movement of gold, is important from the viewpoint of the maintenance of the gold standard. If the free movement of gold were not permitted, exchange rates would move erratically and the benefits of the gold standard would be vitiated.

Another important provision, contained in the original monetary law, was that individuals might present gold for coining, paying a brassage charge of one per cent. The free coinage of silver was not allowed, and it was provided that the amount of silver money was never to exceed twenty per cent of the value of the gold coin. The Government was directed to provide a minimum currency of twenty colones per inhabitant, which would mean, with a population of about 310,000 in 1900, a total currency of 6,200,000 colones.

The formulation and introduction of the gold standard is an accomplishment of which Costa Rica may well be proud. The plan was carefully thought out and efficiently carried to a conclusion. The value of the unit chosen was close to the actual value of the peso at the time, although there is a question whether it would not have been desirable at the same time to have made the colón correspond to an even portion of the pound sterling or dollar, such as 48.665 cents, one tenth of the pound, or fifty cents, half of the dollar. The size of the unit was well adapted to the needs of the people; the old peso at its original value was too large for the ordinary needs of the Central Americans. The intermediary of gold certificates for installing the plan assisted in financing the reform and in the accumulation of gold coin; it also facilitated the retirement of the bank notes without a contraction of the currency. The

law was deficient in not providing for redemption in gold of the silver money, which was now fiduciary. However, this omission was never the source of embarrassment, and the limitation of the amount of silver to twenty per cent of the gold coin provided a safeguard against redundancy.

Costa Rica is the only country which took deliberate means to rid herself of the old foreign coins; in Guatemala and Nicaragua they were driven from circulation by paper money; and in Honduras and Salvador they were drawn from the country by high prices for silver during the war. Honduras did not take adequate measures to prevent a large number of the coins from returning to circulation. Costa Rica was also the first of the countries definitely to adopt the gold standard and to carry through to a successful conclusion a comprehensive monetary reform.

From the inauguration of the gold standard in 1900 until the outbreak of the European war in 1914 the monetary history of Costa Rica was relatively uneventful. The country enjoyed the benefits of the gold standard during this period, and exchange rates were relatively stable. Gold moved in and out of the country according to need, and there were no great fluctuations in exchange rates. The years 1901 and 1902 were bad years for the coffee growers, and the Government's revenue diminished to the extent that the Government defaulted in the payment of interest on its foreign debt.[7] The outbreak of the war in 1914 which disrupted most of the markets of the world, forced Costa Rica to resort to the expediency of irredeemable paper money, which marks the beginning of another chapter in her monetary history.

[7] These payments were not resumed until the refunding operations of 1911.

Chapter XVII

CURRENCY SYSTEM AND THE WAR

1. *Crisis of* 1914

THE European crisis of 1914 fell with especial severity upon Costa Rica. She was unfortunate in having her prosperity closely tied up with a single industry, the coffee industry, and in having this coffee shipped chiefly to one market, England. Costa Rica is an agricultural country, and the most important crop is coffee; the commercial life of the country centers around coffee as in the other Central American countries. England had long been the best market for Costa Rican coffee and normally received seventy-five or eighty per cent of the total product.

The banana industry is also one of great importance to Costa Rica, but this industry is almost wholly in the hands of foreigners and is carried on with foreign capital, so that it stands somewhat apart from the rest of the trade of the country. Very few bills of exchange due to banana shipments go through the exchange market; the domestic payments of the banana companies are largely to pay for local operating expenses, and only a small percentage of their income, which is received abroad, and mostly in dollars or pounds, is converted into colones locally. To obtain colones for local expenses the companies sell drafts on New York or London. The bananas are sent mostly to the United States so that this trade was not greatly disturbed by the opening of the war.

Before the war most of the bills of exchange were in pounds sterling because of the coffee which went to England. However, dollars drafts were not uncommon and there was always a ready demand for either pounds or dollars. The coffee crop for the year 1913-1914 was one of the largest on record. When the war broke

out the shipments for that season were practically completed, as was also the financing of the crop. After the war commenced British financial interests began calling in all their available funds and ceased extending credits. The demand for drafts on London became intense in Costa Rica, and as a result the rates began to rise. Soon there was such a scarcity of drafts that it was almost impossible to purchase any, either in dollars or pounds, and many merchants were unable to settle their foreign obligations.

Gold began moving out of the country and the notes of the four banks of issue were presented for redemption in gold so that the gold might be exported and drafts drawn against it. To relieve the banks of this situation and to prevent an excessive contraction of the currency, a moratorium on the redemption of notes was given the banks on September 18, 1914, to last until further disposition. The banks were not required to redeem their notes in gold, and the notes were made payable for all obligations contracted in gold colones. Thus began the régime of inconvertible paper money in Costa Rica. But it was not the notes of these banks which was to form the bulk of the circulating medium as will be noted later. To prevent any more gold from leaving the country a law was passed in November which prohibited the exportation of any gold or silver coin; gold and silver from the mines, however, might still be shipped out.[1]

2. *Government Bank organized*

The next move on the part of the Government was to organize the Banco Internacional, a government bank which was to extend credit to the hard-pressed producers and ease the stringent situation generally, also to assist the Government since its revenues had fallen off decidedly. The checkered history of this bank constitutes the

[1] This law was repealed in June 1921.

outstanding feature of Costa Rican finance during the period of the next few years. The bank was founded by executive decree of October 9, 1914. It was well received and started on its way auspiciously. The decree provided for a board of directors of seven members appointed by the President, but who governed the bank with complete independence of the Executive. They elected the officers of the bank and were alone responsible for its management. The capital of the Bank was contributed by the Government in the form of bonds, an unused portion of the refunding bonds of 1911, which the Government still had and which amounted to a little over two million colones. The bonds were a first lien on all customs duties and were deposited in the National City Bank in New York.

The bank was authorized to issue notes to the amount of four million colones. The notes were to be guaranteed by the bonds deposited in New York, together with Treasury bonds of 1914 which were guaranteed by custom duties and by the national income from liquor. Arrangements for issuing these latter bonds were made contemporaneously with the organization of the bank. The law provided that the bank accumulate a gold reserve by utilizing its net profits to import gold from abroad. The bank was to loan two million colones of the notes to the Government against the above Treasury bonds. The other two million were to be available to the public as an emergency fund, "and are especially for the purpose of sustaining the sources of the national wealth, assisting the harvesting of the crops, the production of grain, the activities of the mills and factories, and the important necessities of commerce. The coffee exporter whose credit has been suspended by the European conflict, or diminished to such an extent that he may suffer serious damage, may solicit from the bank whatever is necessary to cover the expenses of his finca and the advances to the workers, provided that he show how he dispose of such current credits, and that he be in the conditions indicated, and that his crops and coffee purchased

be sufficient to cover the amount solicited."[2] Loans to individuals by the bank were not to carry an interest rate higher than ten per cent.

The notes of the Banco Internacional were to be received in the government offices on the same basis as the other notes. All obligations contracted in colones the payment of which creditors did not desire to accept in the new bank notes, were granted a moratorium until one year after the signing of peace in Europe.[3]

These are the chief features of the new bank and it can be seen that it was strictly a government institution. The Government provided the capital in the form of its own bonds, and the bank was managed by government appointees.

To provide assistance for the small farmers the original law provided that the bank loan a certain amount of money to the small landowners in the form of rural credits.[4] An additional law was

[2] *La Gaceta, Diario Oficial*, Oct. 10, 1914. Decreto No. 16, artículo III.

[3] The conversion of the notes was to begin one year after the signing of peace in Europe.

[4] Costa Rica differs from the other Central American countries in a peculiar way as regards small farms and landowners. In the other countries, especially Guatemala and Nicaragua, there exist a few wealthy individuals, a sort of landed aristocracy, who occupy a dominant position and control a large area of the land of the country. In Costa Rica, on the other hand, this condition has never existed. When the Spanish settlers arrived they found a sparsely populated country, and the few tribes not well adapted to form a serf class. The Indians were in a low stage of civilization and not accustomed to continued labor, with the result that when they were enslaved and treated with cruelty, their number decreased rapidly and the Spaniards were forced to do their own labor. This accounts for the fact that the present population of Costa Rica is predominantly of Spanish descent. The settlers were unable to live in towns and be supported by Indians working on their lands, but on the contrary were forced to make their homes in the country and provide their own sustenance. These conditions have had a marked effect upon the history of the country and today, on the central plateau on which practically all of the inhabitants live, the land is divided up into a large number of small farms cultivated by small landowners. There are few individuals in Costa Rica of especial wealth.

passed in December, 1914, directing the Banco Internacional to establish in the different districts agencies known as "Juntas de Crédito Agrícola." Each Junta was to be composed of from three to five local farmers who would loan out the money among their neighbors, not giving more than 250 colones to any single individual. The bank proceeded to organize a number of these agencies throughout the country and allocated a certain portion of its funds to be loaned through them to the small landowners. At the first of 1923 the bank reported that it had not yet lost a cent from loans through any of the Juntas.

3. *Operations of the bank*

The bank opened its doors in November 1914 and began doing a regular banking business. During the first few years of the bank's existence its affairs were managed conservatively. At the end of its first year it had accumulated out of net profits a gold reserve of 341,000 colones, three-fourths of which was in foreign gold converted into colones at the legal rate. Including silver and notes of other banks its total cash amounted to 685,000 colones, giving a ratio to notes and sight deposits of about nineteen per cent. At the end of its second year, October 30, 1916, the gold reserve had risen from 341,000 to 750,000 colones, and total cash to 1,445,000, giving a ratio of thirty-three per cent. It was expected that by one year after peace was signed in Europe the bank would have accumulated a sufficient gold reserve, aside from the bonds deposited in the National City Bank as security, to begin redeeming its notes on demand. In 1917, however, after the revolution of January in which Tinoco assumed the presidency of the country, the policy of the bank was changed; it became one of inflation and the bank became subservient to the needs of the administration.

It will be remembered that the law provided that the bank utilize all its net profits in the accumulation of a gold reserve. One of the

first acts of Tinoco was to issue a decree, April 3, 1917, suspending this provision of the law and declaring that the profits already accumulated and those accumulated in the future might be disposed of in any way that the institution saw fit. As a result of the changed policy the cash ratio for October 31, 1917, the end of its third year, dropped to twenty-four per cent from thirty-three per cent the previous year. This was due to a depletion of reserves rather than to an increase in demand liabilities. The gold held by the bank fell from 750,000 colones to 386,000 during this year, and the total cash from 1,444,000 to 980,000.

Payments on the English debt fall due on the first of the year, and as January 1, 1918, approached, Tinoco desired to use the gold in the bank to meet this payment. The directors of the bank refused to give up the gold and all resigned their charges. Their action was accepted and a new directorate appointed on December 8, 1917. On the same day a decree was passed which provided that the gold be appropriated, and that the bank be reimbursed through certificates based on a tax on coffee exports.

In addition to depleting the reserves of the bank, the note circulation was greatly expanded. A decree was issued in October, 1918, authorizing the bank to increase its note issue by the amount of ten million colones, and authorizing all banks of emission to issue notes of small denominations, even as low as twenty-five céntimos, thus enlarging the field for the paper. Of the ten million colones in new notes, four millions were to be loaned to individuals at an interest rate of eight per cent, and six millions were to go to the Government without interest. In June of the following year, 1919, another emission, this time of fifteen million, was authorized; ten million of which were to go to the Government; four million were to be loaned to individuals, and the remaining one million was to be used for repairing the public roads.

Shortly after this decree was issued, and before its provisions had

been fully carried into effect, came the overthrow of the Tinoco Government, September 1919. This ended the period of extravagant finance. Then followed a period of relative conservatism more in keeping with Costa Rican traditions and temperament. The following table shows the position of the bank at the end of each year of its existence and the effect of the Tinoco régime upon it, also how the bank is again getting upon a more solid basis:

BANCO INTERNACIONAL, CONDITION ON OCTOBER 31

	GOLD	TOTAL CASH[5]	NOTES IN CIRCULATION	SIGHT DEPOSITS	GOVERNMENT UNFUNDED DEBT TO BANK (DEC. 31.)
1915	C 340,690	C 685,016	C2,823,200	C 661,904	....
1916	750,074	1,444,558	3,520,100	801,958	....
1917	385,899	980,678	3,217,600	946,345	C 623,610
1918	453,944	629,370	4,833,000	380,762	2,510,693
1919	618,805	824,043	16,441,000	1,555,776	13,030,020
1920	1,006,849	1,079,195	14,337,200	927,832	12,370,200
1921	1,080,526	1,145,265	13,847,000	1,788,566	12,339,000
1922	1,280,455	2,682,689	15,539,500[6]	2,376,737	11,873,000
1923	1,326,757	3,473,736	16,308,276[6]	2,260,584	11,699,000

It will be noted that the gold and cash were both built up during the first two years of the bank's operation, ending October 1916. During the next three years when the Tinoco Government was in power, the position of the bank was greatly weakened; the note circulation was increased many fold as was the debt of the Government to the bank; the gold and cash reserves also were depleted. Recent years show how the condition of the bank has been improving.

Before Tinoco left the country he received from the Royal Bank of Canada gold and drafts on New York and London, the bank receiving in return notes of the Banco Internacional. This trans-

[5] Includes notes of other banks, silver certificates, subsidiary money and checks on other banks.

[6] This increased circulation is explained on p. 216.

action came to be the source of a long controversy since the notes were repudiated by the new Government. There were various irregularities in the transaction and it appears that the legal formalities were not fully complied with. The Government kept all its funds with the Banco de Costa Rica which was its agent by a long standing contract. The Minister of Finance presented to the Royal Bank a check on the Banco Internacional which paid the Royal Bank in notes of one thousand colón denominations. These notes were somewhat irregular in form since the bank at the time lacked the proper blanks. In a few days Tinoco fell, and left the country, taking the money received from the Royal Bank, supposedly somewhere between two and three hundred thousand dollars. The new Government then refused to honor the notes maintaining, among other things, that the Royal Bank must have been aware of the situation and should not have assisted Tinoco to finance his escape. The Royal Bank, on the other hand, maintained that the documents in its possession constituted a clear claim on the bank, and that there was nothing improper in the transaction to warrant repudiation.

One of the first acts of the new administration was to grant to the Banco Internacional and to the Public Treasury a moratorium of one year for the payment or repudiation of the checks of the previous Minister of Finance. In August 1920, about one month before the year expired, a decree was issued nullifying the various acts of the Tinoco administration, including the notes given to the Royal Bank and which the bank still held, also repealing the authorization for an issue of fifteen million colones by the Banco Internacional. The Royal Bank prosecuted its case in the local courts but was not able to obtain a favorable decision. It secured the aid of the British Government, and the matter was submitted for arbitration to a commission presided over by Chief Justice Taft of the United

States. A decision was rendered in October 1923 favorable to Costa Rica and against the Royal Bank. The notes given the bank were declared invalid.

4. *Silver currency debased*

THE national silver money was altered during the period of the Tinoco Government in order to take advantage of its increased bullion value due to the rise in the price of silver. In July 1902 a decree authorized the executive to issue silver certificates of one and two colones against deposits in the Treasury of an equal amount of national silver money, the certificates to be redeemable on demand in the silver money. A large number of these silver certificates had been issued in accord with this law, and circulated freely with the other money.

The silver coins were fiduciary as noted in the previous chapter.[7] However, when the price of silver advanced, beginning in 1915, and when exchange rates rose due to the prohibition on exportations of gold and to the inconvertibility of the bank notes, it became profitable to export the silver coin and draw drafts against the proceeds of its sale. When the price of silver is at eighty cents an ounce, United States currency, the silver in two fifty-céntimo pieces is worth approximately one gold colón. When the price of silver goes above this point the bullion in the silver coins is worth more than the monetary value of the coins.

However, since exchange rates at this time were considerably above par, the value of the silver money if exported abroad became worth more than its domestic monetary value before the price of silver in New York reached eighty cents an ounce. In fact withdrawal of the silver coins from monetary uses in Costa Rica was made profitable by the rise in exchange rates and local depreciation of the paper money, independently of the rise in the price of

[7] The fifty céntimo piece, the largest silver coin, contained 10 grams of silver .900 fine as arranged by the law of 1900. cf. p. 190.

silver, although this fact was not commonly recognized. With exchange rates on New York at a point where 2.60 colones equal one dollar, instead of 2.15, or par, the colon was worth only about thirty-eight and one-half cents. At this rate of exchange whenever the price of silver is above about sixty-six and one-half cents an ounce the value of the coins as bullion in foreign markets is greater than their value as colones in Costa Rica used, we will say, in purchasing drafts on New York. From the first of 1915 until about April 1917 exchange rates were fluctuating in a general way around 260, although for the first month or two in 1916 they were down around 225. In the early part of 1917 they began going up and by the end of the year were above 500; for 1918 they averaged about 450.

It can be seen that had the price of silver remained around its previous ten-year average of about fifty-nine cents, high exchange rates alone would have made the exportation of the silver coins profitable. Conversely, had there been no advance in exchange rates, the high price of silver would have provided an incentive to withdraw the silver coins from circulation. The price of silver began going up in the latter part of 1915 and for the year 1917 averaged about ninety cents; for 1918 about ninety-eight cents and for 1919 about $1.12. The two forces together made withdrawal doubly profitable.

The exportation of silver or gold money, it will be remembered, was prohibited by the law of November 1914. Nevertheless both of these metals soon began to disappear from circulation. The prohibition on exportation prevented the taking of full advantage of the greater value of the coins in foreign countries, but it could not prevent their withdrawal from circulation. Some money was exported clandestinely but more was hoarded since its increasing value in terms of local paper, and its metallic character with a commodity value of its own, made it especially desirable for hoarding.

During the year 1917 a scarcity of silver money became apparent and in order to provide a sufficient amount of small money and to permit the Government to receive the benefit of the increased value of the silver coins two laws were passed. The first, in June 1917, authorized the issuance of silver notes, *billetes de plata*, with a metallic reserve of only forty per cent. The existing silver certificates had a reserve of 100 per cent, and the new law provided that these be recalled and exchanged for the new notes. The second law, passed in September 1917, authorized the coining of silver of a fineness of only .500 instead of .900 as the original monetary law provided, and which was the fineness of the existing coins. Thus by these two laws a considerable debasement of the currency was effected. A large portion of the old silver coins was held by the Banco de Costa Rica acting as agent for the Government, and was a reserve for the silver certificates, which circulated in its stead. Only a very small amount of the new coins .500 fine were actually minted, and the reserve needed for the new silver notes—only forty per cent—was kept in the old coins but computed on the basis of coins .500 fine.[8]

In order to complete the withdrawal of the old certificates, in October 1918 the Government agreed to redeem them for a three months' period—extended later—at their legal par of forty-six and one-half cents gold, their silver value at the time was about fifty-nine cents, or to receive them for custom duties which were payable in gold.[9] In October 1918 the silver notes were given full

[8] In 1923 and 1924 the old coins were restamped or reminted at double their face value. cf. p. 217.

[9] The foreign price of silver in October 1918 averaged about $1.02. Since one colón in silver money contains 18 grams of pure silver the value of the silver in the colón was about 59 cents. However, exchange on New York in October 1918 was about 480 so that 59 cents in New York would sell for about 2.83 colones in Costa Rica. Thus the "fiduciary" silver money was worth nearly three times the paper money due to the rise in the price of silver and the rise in exchange rates.

legal tender on the same basis as the notes of the Banco Internacional.[10] With the price of silver at over a dollar an ounce it can be seen that these operations were very lucrative to the Government.

Amount of Paper Money in Circulation
Guaranteed by Silver

		SILVER CERTIFICATES	SILVER NOTES
1915	Jan.	C1,014,000	
	July	1,014,000	
1916	Jan.	961,000	
	July	829,850	
1917	Jan.	858,300	
	July	773,050	C 27,500 (Sept.)
1918	Jan.	534,000	618,750
	July	353,700	1,850,000
1919	Jan.	160,380	3,272,250
	July	154,480	3,272,250
1920	Jan.	154,380	3,272,250
	July	154,380	3,272,250
1921	Jan.	154,380	3,272,250
	July	116,230	3,272,250
1922	Jan.	116,230	3,272,250
	July	116,230	3,272,250
1923	Jan.	101,520	2,406,250
1924	Jan.	97,400	1,102,220
	July	96,170	899,860

5. *Note issue of non-Government banks*

When the war commenced in 1914 there were four banks in Costa Rica, exclusive of the private bankers and commission houses.[11] The Banco de Costa Rica originally enjoyed a monopoly of note issue, but by a contract in 1896 it renounced this privilege, and all four

[10] cf. p. 212.

[11] The banks of Costa Rica and the dates of their foundings are as follows: Banco Anglo-Costarricense, 1864; Banco de Costa Rica, 1877; Banco Comercial, 1904 (failed the last part of 1914); Banco Mercantil de Costa Rica, 1908 (affiliated with Mercantile Bank of the Americas, which has been reorganized under the name Bank of Central and South America); Banco Internacional, 1914; Royal Bank of Canada, 1915.

of the banks in existence in 1914 had notes in circulation guaranteed by a minimum gold reserve of forty per cent. We have noticed how during the first few weeks of the war the banks were heavily drawn upon for gold, and in consequence were granted a moratorium on the redemption of their notes. The notes were made payable for all obligations contracted in gold colones, but certain questions as to their legal tender were not entirely clear. By 1918 the notes of the Banco Internacional had come into being and enjoyed a wide circulation, and to settle any questions as to legal tender, and especially to encourage the circulation of the new paper notes, a law was passed in June 1918 which made all the notes of the banks full legal tender for all obligations contracted or which may be contracted in gold colones. The payment of custom dues was exempted from this decree.[12]

The banks were authorized to issue notes against the Treasury bonds of 1914; these bonds were issued especially to provide security for the notes of the Banco Internacional and were not taken up by any of the other banks. In October 1918 the banks were authorized to issue notes of small denominations, from two colones down to twenty-five céntimos. This again was for the benefit of the Banco Internacional and none of the other banks took advantage of this provision.

The note circulation of the banks, except the Internacional, declined decidedly during the first year of the war, as can be seen from the following table:

[12] The decree of September 1914 read as follows as regards legal tender: "Los billetes de dichos bancos servirán para pagar todas las obligaciones contraídas en colones de oro"; that of June 1918 provided: "Los billetes de dichos bancos tienen en todo caso y por la suma que indiquen valor liberatorio respecto de cualquier obligación contraída o que se contraiga en colones de oro." *Memoria de Hacienda y Comercio*, 1915, p. 12. *La Gaceta*, No. 136. June 18, 1918.

COMBINED CIRCULATION OF PRIVATE BANKS, COSTA RICA

1914	June	C 4,771,900	1919	June	C 2,342,900
1915	"	1,420,500	1920	"	1,313,000
1916	"	3,351,100	1921	"	252,000
1917	"	3,535,600	1922	"	169,500
1918	"	3,136,100	1923	Dec.	143,100

Beginning about the end of 1915 when business had begun to accustom itself to the war-time situation the banks began to expand their circulation. The note circulation continued to increase until after the *coup d'état* in 1917 by which Tinoco assumed the Presidency. Early in his administration Tinoco began to exploit the Banco Internacional as we have already noted. A large portion of the bank's gold was removed, and the provisions arranging for the accumulation of more gold were destroyed; at the same time the circulation of the bank was increased. As the position of the bank was weakened and as the note circulation expanded, confidence in its notes was shaken, and especial favor came to attach to the notes of the other banks, which it was known were guaranteed by a generous gold reserve, over 100 per cent in some cases, and which would be redeemed in full some time.[13] The value of the silver certificates was likewise depreciated, and these, together with the notes of the Banco Internacional, were not considered as valuable as the notes of the three stronger banks. The result was that the more valuable notes were withdrawn from circulation, the banks withdrawing the notes themselves as far as possible.

This is a unique instance of the operation of Gresham's law, the principle here acting upon inconvertible paper currency. None of the paper notes was redeemable, but it was known that certain issues had gold locked up behind them and it was believed that ultimately

[13] The law in 1914 provided that none of the banks detract to any purpose whatsoever any of the gold which they held in their vaults as guarantee for the notes.

the notes would be redeemed at par, a belief which has since proven to be correct. Provisions for the redemption of the notes of the Banco Internacional were no different than those for the redemption of the other notes, the former notes also had a certain amount of gold behind them. But as the issues increased and the percentage of gold reserve became less, prospects of redemption became more remote, and these notes of the Banco Internacional, together with the debased silver notes, came to be the cheapest class of money, and stayed in circulation driving out the better money.

The Banco Comercial, founded in 1904, became involved in difficulties soon after the outbreak of the war. Its affairs became complicated and in the latter part of 1914 the bank failed. It had at this time about two million colones in circulation, and its assets in relation to liabilities were relatively small. The law required that banks of issue maintain a gold reserve of at least forty per cent against the outstanding circulation, but investigation showed that the bank held only a very small amount of gold. The Government came to the assistance of the noteholders and in February 1915 announced that it would guarantee the notes of the defunct bank, retaining the right, however, to reimburse itself out of any assets the bank might have.[14] With the Government behind the notes of the failed bank they continued to circulate, but the amount gradually declining as a portion was retired from time to time.

The moratorium of 1914 on the redemption of bank notes was to last until further disposition. This further disposition came in June 1918 when it was decreed that the inconvertibility should last until March 31, 1921, after which date the banks would be obligated to redeem their notes in accord with the regular banking law, which requires that the banks redeem their notes on demand in gold,

[14] The following year the Mercantile Bank contracted to take over the affairs of the Banco Comercial and to liquidate its business.

either national, or foreign gold at the legal rate.[15] The banks had held continuously a large stock of gold in their vaults, foreign gold in large part, and when April 1, 1921, arrived, experienced no difficulty in redemption. The effect of this redemption upon the amount of notes outstanding can be seen in the reduced figure for June 1921 in the above table.

The Banco Internacional of course was on a different ground. Its gold reserve had been increasing somewhat but the notes were considerably depreciated and redemption was out of the question. Accordingly on March 31, 1921, Congress decreed that the Banco Internacional was not included in the previous disposition, and that its notes should continue inconvertible until a later law. Since the currency consisted almost entirely of notes of this bank and the silver notes, it can be seen that convertibility of the other bank notes, which no longer circulated, was not a restoration of the gold standard.

The private banks were deprived, July 15, 1921, of their right to issue notes, so that the government bank, the Banco Internacional, is now the sole bank of issue. The law arranged that the private banks pay over to the Internacional the gold which guaranteed any of their notes which might not be presented for redemption. At the first of 1923 about 150,000 colones in notes of these banks were still outstanding, and it was believed that most of these had been either lost or destroyed.

6. *Unification of paper currency*

In order to simplify the paper currency of Costa Rica a law was adopted May 19, 1922, which arranged that the only paper money of the country be the notes of the Banco Internacional. This bank had recently been made the sole bank of issue, but there still existed

[15] cf. *supra*, p. 197, for ratings of foreign gold.

the silver notes, guaranteed by a forty per cent silver reserve in coins .500 fine, and the notes of the defunct Banco Comercial. The original silver certificates had been practically all retired. The law now provided that the silver notes of the denominations of 2., 1., and .50 colones, and the notes of the Banco Commercial be presented at the Banco Internacional in exchange for notes of this bank. The Internacional was authorized to increase its circulation to the extent of 4,282,250 colones for the purpose of taking over these other paper notes.[16]

The increased liability of the Banco Internacional in view of these additional notes was taken care of as follows. The bank was to debit the account of the Government the full amount of the new issue, 4,282,250 less the following credits: the market value of the silver in the silver reserve, which reserve was transferred to the Banco Internacional; funds realized from the liquidation of the assets of the Banco Comercial; and the amount of notes which the public might not present for exchange. At the first of 1923 the Internacional had redeemed about two million colones in silver notes and notes of the Banco Comercial, paying out its own notes. This is shown in the increase of the bank's circulation.[17]

The currency of Costa Rica is made up as follows: Most of the currency consists of notes of the Banco Internacional which purport to be redeemable in gold but which have behind them only a small amount of gold reserve. Their security is chiefly the credit of the Government, partly in the form of bonds and partly in unfunded debt to the bank. Owing to their great number, their gold value is considerably depreciated, less than half the previous value, and it

[16] The notes of the Banco Comercial ceased to be legal tender in November 1922 although the Internacional was still required to exchange them for its own notes.

[17] cf. p. 206. On June 30, 1924 notes of the Banco Comercial to the extent of 453,700 colones were still outstanding.

appears improbable that the notes will ever be redeemed at par, although some of the bank officials have held this to be their aim. Along with the notes of the government bank, circulate the silver notes and the notes of the Banco Comercial, on an equivalent basis. These latter two classes of notes are now being retired. There is a certain amount of small brass coins of the denominations of five and ten céntimos which circulate along side of the other money. Since March 1924 notes issued by the Caja de Conversión and redeemable in gold drafts have appeared. These, however, are most all being hoarded. The Caja is discussed below.[18]

A law of July 1923 ordered the silver coins which had been transferred to the vaults of the Banco Internacional by law of May 1922, restamped at double their face value and placed in circulation. Thus the twenty-five céntimo piece became a fifty-céntimo piece, a fiduciary coin. These restamped silver coins began to be placed in circulation in the latter part of 1923. Since many of the coins were worn, and the small denominations were difficult to stamp, a decree in January 1924 ordered that the coins be melted down and new coins minted.

Gold coin, of course, ceased to circulate soon after the outbreak of war in 1914. Its exportation was prohibited, but in spite of this a large amount found its way out of the country. That which remained in the country was either locked up in the vaults of the banks or was hoarded. A certain amount of American money, chiefly paper, has been brought into Costa Rica but does not circulate as it does in some of the other Central American countries. A large part of this money was exported during 1921 and 1922. A certain amount of business, however, is transacted in terms of American dollars, in order to escape the difficulties attendant upon the fluctuating value of the colón. The fate of the notes of the non-government banks and of the silver certificates has already been described.

[18] cf. p. 231.

Chapter XVIII

FOREIGN TRADE AND EXCHANGE RATES

1. *Factors in foreign trade*

COSTA RICA is a tropical country, and her most important products are coffee, bananas, sugar, precious metals, hides, hard woods, cacao and rubber. The first in importance of these, from the point of view of total value and from that of importance to the people generally, is coffee. Coffee is the crop upon which the prosperity of the country chiefly depends. The coffee plantations are held almost universally by natives, although some of the better ones are getting into the hands of foreigners. This tendency for the more valuable plantations to pass into the hands of foreigners has been increasing in recent years. The coffee is usually marketed by the planter himself who ships his coffee directly to an importer in the foreign country, or sometimes on consignment to an agent who sells the coffee in the open market. The practice, common in Guatemala, of selling to commission houses which buy the coffee from the local growers and export it on their own account, is not the usual procedure in Costa Rica.

As regards value, second to coffee come bananas. The banana industry is one of recent and growing importance. A few decades ago the banana was almost unknown outside of tropical countries, and was not an article of commerce. Its cultivation was begun in Costa Rica in connection with building a railroad to the interior, and proved to be a profitable proposition. Cultivation was also undertaken in Jamaica and the West Indies, and the bananas were sent to the United States where the fruit came into popularity. The chief market for bananas is the United States, and it is only recently that Europe has been consuming them in any quantity. The

industry in Costa Rica, as in most all the Caribbean countries, is in the hands of the United Fruit Company, which has grown to large proportions and controls most of the railways of Central America as well as a line of steamships operating between Central American ports and the United States. It is a strong company and has an important influence in all the Central American countries. Since the banana industry is mainly in the hands of foreigners, it is not of as great interest to the country at large as is the coffee industry; however, many of the natives own banana plantations and sell the fruit to the Fruit Company.

There are a few gold and silver mines in Costa Rica, and the exportation of the precious metals would rank third or fourth in the list of the country's exports. As for sugar, hides, hard woods, cacao and rubber, these articles are of less importance as compared with coffee and bananas.

Another factor affecting Costa Rica's foreign trade, of less importance, however, is the annual expenditures of tourists in the country. San José, the capital of Costa Rica and the most important city, is more accessible to American tourists than most of the other cities in Central America, and during the months from early winter until late spring has become a popular place for tourists. The country is naturally an attractive country. The tourists cash drafts, usually on New York, which drafts affect Costa Rica's trade as do drafts drawn against exports of actual goods.

The imports of Costa Rica are those of any tropical country having almost no manufacturing industries of its own. The imports are of a widely diversified nature and comprise numerous manufactured articles, and certain food commodities. These are machinery, tools for agricultural purposes, iron and steel manufactures, cotton goods and other textiles, boots and shoes, lard, wheat flour, and miscellaneous food products. The imports into Costa Rica come

chiefly from the United States. Great Britain ranks second, but during the war the goods came almost entirely from the United States. Since the close of the war Costa Rica is again buying a large portion of her goods from Great Britain, and a certain amount from continental Europe.

Costa Rica has long had an excess of exports over imports as can be seen from the accompanying table. The cause of this excess is found in the large amounts of foreign capital invested in Costa Rica upon which interest and dividend payments must be made.

Imports and Exports of Costa Rica

	IMPORTS	EXPORTS	EXCESS OF EXPORTS
1900	C 6,300,000	C 6,300,000	
1901	4,400,000	12,200,000	C 7,800,000
1902	4,900,000	12,100,000	7,200,000
1903	5,500,000	15,700,000	10,200,000
1904	6,000,000	15,100,000	9,100,000
1905	5,200,000	17,400,000	12,200,000
1906	14,600,000	18,900,000	4,300,000
1907	16,000,000	19,500,000	3,500,000
1908	12,100,000	16,700,000	4,600,000
1909	13,100,000	17,600,000	4,500,000
1910	17,000,000	18,000,000	1,000,000
1911	19,100,000	19,200,000	100,000
1912	21,700,000	21,400,000	300,000*
1913	18,700,000	22,200,000	3,500,000
1914	16,200,000	23,400,000	7,200,000
1915	9,600,000	21,400,000	11,800,000
1916	14,200,000	24,000,000	10,200,000
1917	12,000,000	25,500,000	13,500,000
1918	8,000,000	20,700,000	12,700,000
1919	16,200,000	38,200,000	22,000,000
1920	38,100,000	26,800,000	11,300,000*
1921	19,700,000	25,600,000	5,900,000
1922	17,900,000	30,600,000	12,700,000
1923	21,040,000	27,600,000	6,560,000

*Excess of imports.

Principal Exports

	1922	1923
Coffee	C 14,400,000	C 10,125,000
Bananas	10,800,000	11,181,000
Cacao	1,980,000	2,345,000
Gold and silver	1,100,000	1,257,000
Sugar	430,000	1,133,000
Miscellaneous	1,890,000	1,559,000
TOTAL	C 30,600,000	C 27,600,000

The external debt of the Government at present amounts to about thirty million colones. To be added to this is the private capital invested in various forms in the country, the total amount of which cannot be definitely determined, but the chief item of which consists of the investments of the United Fruit Company.

The chief source of drafts in Costa Rica is from shipments of coffee, and from the banana companies which sell drafts to pay wages and other local expenses. These drafts are bought by the banks and brokers who dispose of the funds to the local merchants and importing houses who have foreign payments to make. Some of the larger houses handle their own financing, and do a small business in dealing in exchange on the side. The bulk of the business, however, is done by the banks, the private bankers and the commission houses.

2. *Foreign trade and exchange rates during the war*

According to gold parity the Costa Rican colón is normally worth about forty-six and one-half cents in American money, or, since exchange rates are usually quoted in terms of the number of colones to the dollar, a rate of 215—*i.e.*, 2.15 colones to the dollar—means that exchange is at par. After the gold standard was inaugurated in 1900 fluctuations in exchange rates were not very great. A slight rise in the rates in 1908 was caused by an exception-

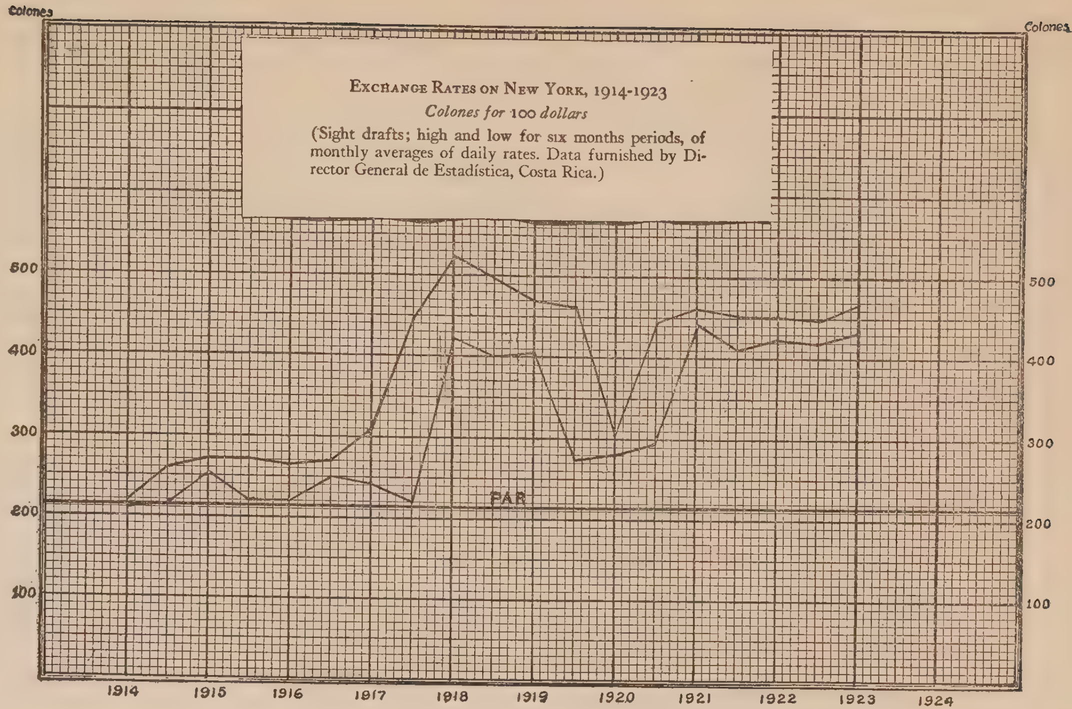
ally poor coffee crop that year, about one-half that of the previous years, with the result that drafts on London and New York were scarce and their prices high.

When the war began in 1914 exchange rates were approximately at par, but they immediately began going up due to the cutting off of foreign credits and the calling home of funds by London and the continent. The demand for drafts became intense and exchange rates mounted rapidly. As the available supply of drafts was taken up, the position of persons with payments to make in London became difficult, and many were embarrassed in meeting their obligations. Gold began to leave the country, and the bank notes were presented at the banks for redemption in gold. This was stopped by the moratorium on redemption of bank notes, already noted, which was decreed in September 1914, and by the embargo in November on the exportation of gold and silver coin. Exchange rates on New York rose from about 215 in July 1914 to around 260 at the end of the year, as is shown in the following chart. The country's trade was completely disrupted by the war, and the rates continued to rise during 1915 reaching about 270 by the middle of the year.

As the foreign trade shifted by necessity from Europe to the United States, dollar drafts came to predominate. The method of quoting exchange rates changed from in terms of sterling to in terms of dollars; "exchange" now meant rates on New York.

In November and December 1915 the rates declined noticeably and remained low during the first part of 1916. The coffee crop was exceptionally good this year, as also were coffee prices; we thus find a decline in exchange rates. Normally Costa Rica sent the great bulk of her coffee to England, and the United States received only a very small share. In 1916, however, the United States received almost the same amount of coffee from Costa Rica as did England.

CHART V



Colones
Colones
Exchange Rates on New York, 1914-1923
Colones for 100 dollars
(Sight drafts; high and low for six months periods, of monthly averages of daily rates. Data furnished by Director General de Estadística, Costa Rica.)
500
400
300
200
100
PAR
1914
1915
1916
1917
1918
1919
1920
1921
1922
1923
1924

The currency was not greatly increased in amount until after the beginning of the Tinoco administration in 1917, and judging by exchange rates and local commodity prices, which appear not to have increased to any great extent during the early years of the war, it cannot be said that the currency of Costa Rica was especially depreciated at this time, although it was irredeemable and there were no immediate prospects for a resumption of specie payments. However, beginning in the spring of 1917 the situation changed; exchange rates rose precipitously and there was general uneasiness. An interesting point to observe in this connection is that the rise in exchange rates was prior to the great increase in paper notes put out by the Banco Internacional; it was in a sense anticipatory of the inflation to follow. When the increase in currency later took place it was not followed by a rise in exchange rates.

The explanation for this seeming inversion appears a little obscure. The coffee crops of 1917 and 1918 were somewhat under normal, but more than offsetting this, prices for coffee were unusually good, and we can find no explanation for soaring exchange rates in this direction. Total exports in 1917 were larger than ever before, and imports somewhat less than the previous year; however, it might be added that a large part of the increase in exports was in banana shipments, bills for which do not ordinarily go through the exchange market.

The reasons for the sudden rise in exchange rates in the spring of 1917 seem to have been as follows: First, in April of this year the United States entered the war. This resulted in an immediate curtailing of credits, and a calling in of funds, which naturally tended to push up the rates. Combined with this was general apprehension as to the future. The Tinoco Government was not starting off auspiciously; it did not gain recognition by the United States Government, and its financial policy was received with some

suspicion and disapproval. These fears soon were seen not to have been unfounded. The Government's internal debt increased during 1917 from 13,900,000 on January 1 to 19,500,000 on December 31. These increased expenditures of the Government without an accompanying increase in ordinary revenue, tended to bid up prices and to raise exchange rates. Nevertheless the fact that the rise in exchange rates in the brief period of eight months, taking place prior to inflation of the currency and with exports exceptionally large and imports less than the previous year, should have been so tremendous, from about 245 in May to about 440 in December, and 525 in January 1918, is somewhat surprising.

Exchange rates continued high during 1918 and most of 1919, with wide and erratic fluctuations. After the Armistice in November 1918, optimism prevailed and prospects of renewed trade activity caused a recession in the rates which continued for several months' period. In the spring of 1919 they began rising, but declined again in the fall of the same year. The rates moved very erratically during this year, due chiefly to the threatening inundation of paper money, and to the precarious financial policy of the Government. A precipitous fall took place in the month of September 1919, from about 420 at the first of the month to 285 at the last of the month.

This sudden fall in rates is quite as phenomenal as was the rise in 1917. It was in September 1919 that the Tinoco Government was overthrown and that a more conservative administration came into power. This alone had a very salutary effect upon exchange rates. Another cause for the fall in rates was the increase in the value of exports and the resultant increase in drafts for sale. The increase in exports was not so much an increase in physical quantities as an increase in value of the goods exported. The sugar and coffee crops were both good and in addition prices were exceptionally high. Never before had coffee prices been so high. The value of the cof-

fee exports rose from about eight million colones in 1918 to over twenty-five million in 1919. The nearest approach to this was in 1914 when coffee exports reached ten million colones. Imports were increasing during this period, partly as a reflection of increased exports. This tended to check the fall in exchange rates.

The destination of the coffee for the two years 1918 and 1919 shows strikingly the effect of the ending of the war upon Costa Rica's foreign trade. In 1918 when the war was still in progress the United States received over ninety-six per cent of Costa Rica's coffee, and England which before the war had received the great bulk of the coffee, received less than one per cent. In 1919, however, England received about fifty-three per cent and the United States only forty per cent; in 1920, England forty per cent and the United States fifty-seven per cent; in 1921, England forty-six per cent and the United States forty-eight per cent; and in 1922 England fifty-nine per cent and the United States thirty-four per cent.

The high exchange rates during 1918 caused a marked falling off in imports. Shipping difficulties and the entry of the United States into the war were also responsible for a share of this decrease. Imports declined in 1918 to eight million colones from twelve and fourteen million the two previous years, and from around eighteen or twenty million for the years prior to the war. It should be borne in mind that the gold value of the colón varied widely during these years so that comparisons are apt to be misleading. In 1919 imports amounted to over sixteen million colones and in 1920 to thirty-eight million, part of which increase was due to high prices abroad rather than to increased quantities imported. The United States has long been the leading country for Costa Rican imports and in 1919 was the source of about seventy-eight per cent of the imports as against fifty-eight per cent in 1918. The large percentage was due chiefly to the fact that economic conditions in the United States

were less disturbed than in Europe. In 1920 the percentage was fifty-two, in 1921 fifty-five, and in 1922 it was sixty-one, which shows a decline from the high war time amount.

3. *Depression of* 1920-1921

THE coffee crop for 1919-1920 was good and coffee prices remained high; consequently exchange rates were low relative to their previous position. They fluctuated between 280 and 300 colones for $100 during the first seven months of 1920. However, in the fall of the year a change took place. As coffee and sugar prices fell exportations did not realize the anticipated values, and with less foreign bills for sale the price of bills began to rise. Exchange rates continued to rise and were up around 450 for the first part of 1921. While the supply of funds abroad had diminished, the demand for such funds had increased. The favorable condition of the coffee market had produced a wave of prosperity and importers had been purchasing large supplies of goods to meet the increased ability to buy. Suddenly the coffee market collapsed, commodity prices in foreign countries began dropping, importers found themselves stocked up with goods bought at high prices and which could now be replaced at lower prices. With reduced incomes people were not buying as they had a few months previously. Importers buy their goods ordinarily on credit, and they now found it most difficult to pay. At the same time the price of drafts with which to pay was soaring. Orders were cancelled as much as possible, but many merchants became delinquent in their payments.

The country's circulation had been increased several fold and under the existing circumstances it would have been surprising if exchange rates had not risen to high levels. In fact it is a little surprising that they did not rise higher than was actually the case, since they did not reach the high points touched early in 1918. In the latter part of 1921 as business became more settled, the rates

declined a little and the year ended with rates around 420. The average rate for 1921 was about 443 and for 1922, about 435. In January 1923 the rates mounted suddenly reaching about 500, but by the middle of the year had declined to about 430. In March 1924 the rates declined to below 400 whereupon the Caja de Conversión began operations and has maintained the rates practically constant at about 400 since this time.[1]

No measure of the rise in general prices in Costa Rica has been made, but there is sufficient evidence to show that there has been a decided rise in the general price level, and that this rise has lagged behind the rise in exchange rates. A person selling drafts on New York during the period of rising exchange rates, could realize an amount of colones which would purchase in Costa Rica a greater amount of articles than would normally be possible.

Costa Rica did not suffer from the business depression to the same extent as did some of the other countries. The coffee crop for 1920-1921 was not as deficient as in some of the countries and the price of Costa Rican coffee did not fall as greatly as did that of some of the other grades. Costa Rican coffee is of an especially fine quality and is useful for blending purposes, consequently it always brings a better price than some of the other coffees. The crop for the year 1921-1922 was good, and with good coffee prices business in Costa Rica was enabled to recover from the depression of the previous year. The coffee situation in Costa Rica has continued good, although the 1922-1923 crop was a little under size.

[1] cf. p. 231.

Chapter XIX

PROBLEM OF REFORM

1. *Banco Internacional*

THE problem before Costa Rica at present is the strengthening of the Banco Internacional, and the placing of the currency upon a firm and stable basis. The bank was originally planned as an emergency bank to meet the exigencies growing out of the war and was to go out of existence when the emergency had passed. The decree founding it in 1914 provided that it last during the economic and financial crisis caused by the war, and cease to function thereafter. Soon after its founding, however, it began making long term loans, some of which ran for fourteen years. Its affairs became more and more intricate.

A question which was the source of debate was whether the bank should be liquidated and pass out of existence as originally planned, or whether it should be reorganized, put on a firm gold basis and function as a central government banking institution enjoying as it now does the sole right of issuing notes. The bank unfortunately lost a good deal of its prestige and was looked upon as little more than a "paper bank," not entirely improperly. The bank has been too much of a credit factory for the Government. The Government supplied the capital for the bank in the form of its own bonds. On the basis of the bonds, the bank issued notes, a large portion of which went to the Government in the form of loans. The Government's unfunded debt to the bank is nearly twelve million colones. The notes of the bank are considerably depreciated below the pre-war level for the colón; the paper colón is now (September 1924) worth about twenty-five cents, about half its former gold value.

The difficulties of the bank were a heritage from the Tinoco régime. However, the bank has made commendable efforts to strengthen its position, and according to its balance sheet has been successful in this endeavor. The gold holdings and total cash have been continually increased; for this accomplishment the bank deserves praise. The two years, 1921 and 1922, were arduous ones, and with both private and public income greatly diminished, a phenomenal improvement in the bank's condition was not to have been expected. The future of the bank as a strong government institution now seems probable.

2. *Restoration of the gold standard*

A RESTORATION of the gold standard is a problem that Costa Rica is now facing. The present paper currency, accompanied by violent fluctuations in exchange rates, is very unsatisfactory. Fluctuating exchange rates introduce so much of an element of uncertainty into the import and export trade that merchants and dealers do not know upon what basis to figure their business. Fluctuating rates are the source of much speculation; although this is bad for the country at large, good profits—also losses—are made out of these operations, both by the large houses and by the small dealers who operate along the curbstone at the principal corner in San José. In spite of the seeming stimulus from speculation, the erratic fluctuations in exchange rates are a decided handicap to trade, and the whole country suffers from such a situation although the effects are somewhat obscured. Costa Rica desires to return to the gold standard and no doubt will soon do so. Steps looking in this direction have already been taken.

Many complexities are involved with the question of a return to the gold standard. The present paper colón has a gold value of only about half that of the previous gold colón, and any attempt

to raise it to its former value would be accompanied by many difficulties. The country is getting accustomed to the present level of prices, and to go back to the old level would require a readjustment, inevitably bound up with many injustices, and with much needless confusion to business. It would be a retracing of the difficult years through which the country has already come. The inexpediency of this is commonly recognized, and few desire to go back to the old level. It is generally conceded that such a procedure is out of the question. A more important matter is that of determining what is the present value of the paper colón, and at just what value in gold it should be stabilized, a value that would give the greatest justice to everyone considered, and would be most useful and acceptable to business generally.

A law of October 1922 established in the Banco Internacional what is known as a "Caja de Conversión" for the purpose of stabilizing the colón at the rate of four colones to the dollar. The law provided that the "Caja" buy gold drafts, issuing in return notes redeemable in gold drafts on demand, at the rate of four colones to the dollar. The "Caja" was to receive the income from certain revenues to go into a fund for carrying on its operations of stabilizing the colón at four to the dollar.

The Caja came into active operation for the first time in March 1924. Exchange rates fell early in 1924 due to a good supply of coffee bills, and in March went below four colones to the dollar. This permitted the Caja to commence operations. The Caja began giving out notes in return for gold drafts at the rate of four colones to the dollar and at the end of March 1924 there were 766,700 colones outstanding backed one hundred per cent by gold or by dollar credits in the National City Bank in New York. By the first of August 1924 the circulation of the Caja had increased to 1,381,500 colones. The notes are being hoarded and do not circulate,

since they are redeemable in gold drafts while the other notes are not redeemable. Since the Caja will purchase all gold drafts at the rate of four colones to the dollar exchange rates can not go below this point. On the other hand should exchange tend to go above four colones to the dollar the notes of the Caja, being redeemable in gold drafts, would tend to go to a premium in terms of the other paper money unless all notes were made redeemable in gold or gold drafts. In the meantime stability is being enjoyed, which is of great assistance to importers and exporters as well as to business in general.

A unit equal to twenty-five cents American money has much to be said in its favor. According to exchange rates the value of the colón in terms of foreign gold currency has been fluctuating for some time close to this point. Since wages and general prices ordinarily lag behind exchange movements, a unit of twenty-five cents would make allowance for this fact and assume that the country had not yet fully adjusted itself to a value as low as twenty-three cents. Or, if such adjustment were complete, a slight rise in value might give some compensation to those who had suffered by the previous fall in value; wage earners, for example, would find their colón purchasing a little more, instead of a little less which has been the situation for several years past. A unit of twenty-five cents is an even quarter of the American dollar, and would simplify exchange transactions between the two countries. Furthermore, it is exactly one-half of the Salvadoran Colón, one-half of the Honduran peso, and one quarter of the Nicaraguan córdoba. It is also a close approximation to the English gold shilling which is worth slightly less than twenty-four and one-half cents. A unit the size of twenty-five cents is well adapted to an economy such as that of Costa Rica, where the purchases of most of the people are for articles of small value.

The gold standard means that all forms of money are convertible

in gold on demand, and that gold can flow freely into and out of the country at will. In order to attain this condition the existing paper money might be retained, and made redeemable in gold at the new value, so that any excessive amount of the present currency could be withdrawn from circulation by being presented for redemption in gold. The security for the present paper money is chiefly the debt of the Government to the Banco Internacional. In order that the notes may be redeemable in gold, it is necessary that there be a gold reserve behind them; that is to say the value behind the notes should be converted in large measure into gold. To accomplish this the Government would need to undertake refunding operations and would probably need to borrow money in foreign markets since it is unlikely that sufficient money could be raised locally.[1] In order to undertake redemption a gold reserve of at least thirty-five per cent would be required and with fifteen million paper colones in circulation, this would be a reserve of over five million colones. Assuming the colón were to be worth twenty-five cents this would be equal to $1,250,000. The Government has received the benefit of most of the issues of currency put into circulation, and whatever plan of reform be undertaken, the Government must pay off a large part of its present debt, which is the security behind the existing currency.

[1] A foreign loan of $4,000,000 was nearly consummated in 1922, but the Costa Rican Congress finally failed to ratify it. An internal loan was undertaken in 1923 but met with difficulty.

Appendix A

MONETARY UNITS OF CENTRAL AMERICA

COUNTRY	UNIT	COMPOSITION	WEIGHT AND FINENESS	VALUE IN U. S. CURRENCY	
				Nominal	*Actual, August* 1924
Guatemala	peso	silver (see note in last column)	.25 grams .900 fine	fluctuates with price of silver; worth about 47 cents with silver at 65 cents an ounce.	$ .017 (approx.) (inconvertible paper money since 1897.)
Salvador	colón	gold	.836 grams .900 fine	$ .50	$ .50
Honduras	peso	silver (see note in last column)	.25 grams .900 fine	fluctuates with price of silver; worth about 47 cents with silver at 65 cents an ounce.	$ .50 (approx.) (American money legal tender in Honduras at rate of two pesos to the dollar. Pesos and American money circulate practically at this rate.)
Nicaragua	córdoba	gold	1.672 grams .900 fine	$1.00	$1.00
Costa Rica	colón	gold	.778 grams .900 fine	$ .4653	$ .25 (approx.) (inconvertible paper money since 1914.)

Appendix B

FOREIGN COMMERCE

		EXPORTS		IMPORTS	
Guatemala	1913	dollars	14,440,000	dollars	7,959,000
	1921		12,131,000		10,690,000
	1922		11,646,400		10,751,000
	1923		14,726,000		10,841,000
Salvador	1913	colones	22,528,000	colones	15,246,000
	1921		16,959.000		16,793,000
	1922		32,427,000		15,279,000
Honduras	1913-1914	dollars	3,421,000	dollars	6,625,000
	1920-1921		5,429,000		16,723,000
	1921-1922		5,386,000		12,804,000
	1922-1923		10,016,000		14,342,000
Nicaragua	1913	córdobas	7,712,000	córdobas	5,770,000
	1921		8,071,000		5,310,000
	1922		7,903,400		5,123,000
	1923		11,028,300		7,268,000
Costa Rica	1913	colones	22,200,000	colones	18,700,000
	1921		25,600,000		19,700,000
	1922		30,600,000		17,900,000
	1923		27,600,000		21,040,000

Appendix C

REVENUES AND EXPENDITURES

	REVENUES		EXPENDITURES		
	BUDGET ESTIMATE	RECEIVED	BUDGET ESTIMATE	SPENT	ACTUAL DEFICIT
Guatemala 1922	*P* 274,250,000	*P* 306,810,078	*P* 245,216,000	*P* 348,489,902	*P* 41,679,824
Salvador 1923	*C* 13,465,000	*C* 13,925,000	*C* 13,757,000	*C* 14,865,000	940,000
Honduras 1921-1922	*P* 6,674,900	*P* 7,387,000	*P* 6,674,900	*P* 7,680,400	*P* 293,400
Nicaragua 1922		*C$* 2,659,689		*C$* 2,638,346	*C$* 21,143 surplus
Costa Rica 1923	16,644,900	20,520,548	18,663,508	18,205,368	2,315,180 surplus

Appendix D

NATIONAL INDEBTEDNESS, JANUARY 1, 1923

	INTERNAL	EXTERNAL	TOTAL IN DOLLARS
Guatemala	*P* 145,000,000	£ 1,908,563	$12,175,616 (approximate; *P* at 2 c; £ at $4.86)
Salvador	*C* 20,962,259	*C* 13,296,800[1]	$ 17,129,530
Honduras	$ 3,398,300 (July 31, 1921)	£ 28,651,411 (includes accrued interest; loans in default since 1872 and 1873.)	$139,245,857 (approximate)
Nicaragua	*C*$ 3,383,200 (Feb. 1923)	*C*$ 5,431,581 (Feb. 1923)	$ 8,814,781
Costa Rica[2]	*C* 38,995,310	£ 1,620,049 Frc. 32,269,500	$ 19,558,375 (approximate; *C* at 25c; £ at $4.86; *Frc.* at 6c.)

[1]Salvador concluded in the United States a loan of $6,000,000 at 8 per cent in the latter part of 1923.
[2] December 31, 1923.

Appendix E

MONETARY LAW OF NICARAGUA
MARCH 20, 1912

THE National Constituent Assembly Decrees, that it approves the decree on the Monetary Conversion issued by the Executive Power in Council of Ministers on the 25th of February of the current year in these terms:

Article 1. The monetary unit of the Republic shall be the córdoba, and shall contain one gram, 672 milligrams of gold, nine-tenths fine, and shall be divisible into one hundred equal parts.

Article 2. The gold coins of the Republic shall be as follows:

Ten córdobas, which shall contain 16.72 grams of gold, nine-tenths fine.

Five córdobas, which shall contain 8.36 grams of gold, nine-tenths fine.

Two and a half córdobas, which shall contain 4.18 grams of gold, nine-tenths fine.

Article 3. The silver and minor coins of the Republic shall be as follows:

The córdoba, which shall contain 25 grams of silver, nine-tenths fine.

The half córdoba, which shall contain 12½ grams of silver (eight-tenths fine.

The quarter-córdoba, which shall contain 6¼ grams of silver, eight-tenths fine.

Ten centavos, which shall contain 2½ grams of silver, eight-tenths fine.

Five centavos, which shall be of the weight of 5 grams, of which seventy-five parts shall be of copper and twenty-five parts of nickel.

One centavo, which shall be of the weight of 4 grams, of which ninety-five parts shall be of copper and five parts of zinc.

One-half centavo, which shall be of the weight of 2½ grams, of which ninety-five parts shall be of copper and five parts of zinc.

Article 4. The amount of the coinage of both gold and silver shall be determined by the National Bank, under regulations approved by the Executive; provided, that arrangements may be made whenever it seems proper and desirable, by agreement between the Executive and the National Bank, for the unlimited coinage of gold.

Article 5. The tolerance or allowance for wear, of all the coins of the Republic shall be determined by Executive decree.

Article 6. The National Bank shall have and exercise all the powers granted in the banking concession, attached as Schedule "C," to the Trust and Fiscal Agency Contract entered into between the Republic of Nicaragua and Messrs. Brown Brothers & Company and J. & W. Seligman & Company, of New York, on September 1, 1911, as modified by the Treasury Bills Agreement of the same date.

Article 7. The Minister of Finance shall subscribe, on behalf of the Government of Nicaragua, a sum not exceeding $500,000 of the capital of the National Bank of Nicaragua, authorized by the Treasury Bills Agreement between the Republic and Brown Brothers & Company and J. & W. Seligman & Company, of New York, dated September 1, 1911, and shall pay, in accordance with said agreement, such subscription from the proceeds of the loan provided for in said agreement.

Article 8. The President of the Republic is authorized to arrange with the Bankers named as parties in said Treasury Bills Agreement for the exchange, on or before July 1, 1912, or with the approval of the Bankers at a later date, if deemed proper, of the national currency of Nicaragua for notes of the bank, at a rate to be agreed upon by the President and the Bankers and officially declared not less than three weeks prior to the date agreed upon, and in no event to be higher than fifteen hundred pesos in national currency notes for each one hundred córdobas.

Article 9. The present currency plan is hereby declared to be the plan referred to in Article 8 of the Treasury Bills Agreement of September 1, 1911, between the Republic and Brown Brothers & Company and J. & W. Seligman & Company, as Bankers.

In accordance with the provisions of that agreement the Minister of Finance is hereby authorized, with the approval of said Bankers, to order the United States Mortgage & Trust Company, as trustee, to pay over or set aside, in whole or in part, as may become necessary, the moneys now in the hands of said trustee as said Minister of Finance, with the approval of the Bankers, may determine.

The moneys thus paid over or set aside, together with any addition or increment thereto, shall constitute a fund to be called the Exchange Fund, which may hereafter be made a part of the reserve held against the notes of the National Bank. Said Exchange Fund shall be available and used for the following purposes:

First. To exchange on demand for the gold coin of Nicaragua and the notes of the National Bank of Nicaragua, in sums of not less than five thousand córdobas, or the equivalent thereof in the money of the

United States, at the principal office of said National Bank in Nicaragua, or at such branch offices of the bank as may be designated for the purpose, with the approval of the Minister of Finance, drafts on the said Exchange Fund in the United States or other foreign country, charging a premium of one-half of one per cent for sight drafts and one per cent for telegraphic transfers.

Second. To exchange on demand for the currency of the United States, or of any other foreign country in which a part of said Exchange Fund may be deposited, in sums of not less than five thousand córdobas, or the equivalent thereof in such foreign currencies, drafts on the National Bank of Nicaragua or upon such branch offices as may be designated by said bank for the purpose, with the approval of the Minister of Finance, charging a premium of half of one per cent for telegraphic transfers.

Third. To make exchanges between the notes of the National Bank, the gold or silver coin of the Republic, the currency of the United States, and other foreign currencies, under regulations to be made for that purpose by the National Bank, subject to the approval of the Minister of Finance.

The premiums charged for drafts and telegraphic transfers under this article may be temporarily increased or decreased by the National Bank or by the custodians of the Exchange Fund, under the direction of the National Bank, and may be different between different points; but they shall in no case be fixed higher than one and one-quarter per cent for sight drafts, nor one and three-quarters per cent for telegraphic transfers, except with the approval of the Minister of Finance.

The exchanges above provided for may be made provisionally for and with the existing national currency notes of the Republic, until such date as may be fixed under Article 14 of the Act for the termination of the legal tender quality of such notes and at rates of exchange to be fixed from time to time by the Minister of Finance, with the approval of the Bankers or their representatives.

The amounts received as premiums from the sale of drafts or transfers shall be carried to the credit of the fund herein provided for, which shall bear the cost of such drafts and transfers.

Any drafts against said fund, and any orders for payments therefrom, when drawn and signed by the National Bank of Nicaragua, Incorporated, shall be paid out of said fund by the depositary or custodian thereof. Such drafts or orders shall provisionally, until the bank shall be opened for business in Managua, be drawn and signed by the Minister of Finance, and shall be valid when approved by the Bankers or their representatives.

All of the drafts or orders referred to in this article shall be sufficient warrant to such depositary or custodian for the payments therein called for.

Article 10. Neither the Government, nor any other person, firm or corporation, except the National Bank, shall during the term of the charter of said bank, be permitted to issue paper currency or any other form of obligation payable to bearer and capable of being used for circulation as money.

Article 11. The gold coin of the Republic, the silver córdobas, and the notes of the National Bank shall be receivable for customs and other public dues and shall be legal tender in the payment of debts within the Republic.

The subsidiary silver and the minor coins of the Republic shall be legal tender to an amount not exceeding ten córdobas.

Article 12. The importation of foreign coin shall be subject to the control of the Executive, exercised by decree.

Article 13. The circulation of foreign currencies, whether of paper or of gold, silver or other metals, may be permitted or prohibited by Executive decree.

Article 14. Six months after the official rate of exchange provided for in Article 8 of this Act comes into operation, the National Bank then being ready to issue its notes in exchange for the national currency and coins, the latter currency and coins shall no longer be received for customs or other public dues or be legal tender. The currency and coins remaining in circulation after this date—forged or altered notes excepted—may be redeemed under special regulations approved by the National Bank and the Executive.

Article 15. The Executive may take any measures necessary and proper for carrying out the provisions of this Act and the provisions of the Treasury Bills Agreement dated September 1, 1911, and subsequent amendments thereto, and to enable the National Bank and the Bankers parties to that agreement to better perform any or all the functions therein conferred upon them and to restore and maintain the stability of the national monetary system; the measures taken in this connection by the Executive to have legal effect provided they be not inconsistent with the present law.

Article 16. The counterfeiting of the notes of the National Bank shall be subject to the penalties which are provided by the laws relative to the counterfeiting of money.

Article 17. The Banking Law, promulgated by Executive decree March 6, 1882, and all other Acts inconsistent with this Act are hereby repealed.

Appendix F

HONDURAS, TRANSLATION OF PROJECT FOR MONETARY REFORM

Prepared by Arthur N. Young
Financial Advisor to the Government of Honduras

Article 1. The monetary unit of Honduras shall be the "gold peso" equal to the dollar of the United States of America, of 1.671812 grams (25.8 grains) of gold, .900 fine. The gold peso shall be divided into 100 parts, called "gold cents."

Article 2. The right of coinage is reserved explicitly to the State, and may be exercised through contracts with individuals, companies, or foreign governments. Accordingly the Executive is empowered to effect the coinage specified in the present law in such forms as may be deemed most appropriate.

Article 3. The gold coins of the Republic shall be the following:

DENOMINATION	WEIGHT IN GRAMS	FINENESS	WEIGHT OF PURE GOLD, IN GRAMS
10 gold pesos	16.71812	.900	15.046308
5 gold pesos	8.35906	.900	7.523154

Article 4. The silver coins of the Republic shall be the following:

DENOMINATION	WEIGHT IN GRAMS	FINENESS	WEIGHT OF PURE SILVER, IN GRAMS
50 cents gold	12.50	.900	11.250
25 cents gold	6.25	.900	5.625
10 cents gold	2.50	.900	2.250

Article 5. The minor coins of the Republic shall be the following:

DENOMINATION	WEIGHT IN GRAMS	COMPOSITION
5 cents gold	5.00	75% copper and 25% nickel
1 cent gold	3.11	95% copper, 5% tin and zinc
½ cent gold	2.00	95% copper, 5% tin and zinc

Article 6. The dimensions and designs of all coins of the Republic shall be determined by the Executive Power. The Executive Power shall also prescribe by decree the limit of tolerance of the coins.

Article 7. The new coins of gold, silver, nickel and copper shall be legal tender in the country, and the fiscal offices shall receive them in unlimited quantity; but no individual shall be obliged to receive in each

payment more than twenty-five pesos gold in silver money and fifty cents gold in nickel or copper, except in case of special agreement.

Article 8. The paper money, bank notes, gold and silver coins and fractionary money of the United States shall continue to be legal tender for all payments, but with the same restrictions stipulated in Article 7 in reference to payments between individuals.

The equivalence of one American dollar with one Honduran gold peso and with two of the silver pesos now current is established.

Article 9. The importation into Honduras of foreign moneys of any kind whatever, with the exception of money of the United States of America, is prohibited. Any person attempting to bring these coins into the country shall be subject to the penalty of confiscation of such coins, and other penalties established by the Law regarding Contraband and Fiscal Defraudations. Any person or persons giving information leading to the conviction of a person attempting such illegal importation shall receive a reward equal to 50 per cent of the value of the coins confiscated.

Article 10. The exportation of coined money shall be free.

Article 11. Any person who has contracted an obligation to pay in the silver money formerly current in the country shall have the right to discharge his obligation in Honduran money or money of the United States of America in the form and proportions expressed in Articles 7 and 8.

Article 12. The new silver money and the subsidiary coin with the national symbol shall be deposited in the vaults of the National Bank, or in its absence in another bank which offers sufficient guarantees. These moneys will constitute a special fund managed under the supervision and at the orders of the Government which will dispose of it in conformity with this law.

Article 13. The seignorage profits which may result from the coinage of the moneys specified in Articles 4 and 5 shall be used to constitute a reserve fund to be known as the "Gold Standard Reserve."

The total amount of this reserve, which shall be employed solely for the purposes specified in the law, shall be equal to at least thirty-five per cent of the amount of said money in circulation.

Part of this fund shall be deposited in the National Bank, or in its absence, in another accredited bank of the country, the depository bank being charged with its management.

This part of the fund shall be kept physically separate and managed separately from all other funds of the Bank and of the Government.

The other part shall be deposited abroad at the order of the depository bank of the country, which will make use of it in conformity with this law, and under no circumstances whatsoever shall it be hypothecated.

Article 14. The supervision of the said fund shall be exclusively by a special commission of three members, which shall be called the "Monetary Commission" and of which the Minister of Finance shall be President. The Manager of the National Bank, or in its absence of the bank charged with the custody of the fund in the country, shall be a member ex-officio. The third member shall be chosen by the Chamber of Commerce of the country, and will exercise his functions during a period of two years, eligible for reelection, and will receive ten pesos gold for each session, with a limit of 250 pesos gold annually.

Article 15. The "Gold Standard Reserve" shall be used solely for the following purposes:

(a) To exchange in American or Honduran gold or American paper money the moneys specified in Articles 4 and 5, with the right, however, to employ the methods of redemption specified in paragraph (b) *infra*;

(b) To redeem the money specified in Articles 4 and 5 in drafts on that part of the said "Gold Standard Reserve" held in a foreign country when such money may be presented for redemption in amounts not less than 2,500.00 pesos gold, with a premium equivalent to the expenses of exportation of American money or of Honduran gold;

(c) To give the money specified in Articles 4 and 5 in exchange for American or Honduran gold or for American paper money;

(d) To use the money specified in Articles 4 and 5 to purchase drafts which shall be credited to that part of the "Gold Standard Reserve" held abroad, when such drafts are offered in amounts not less than 2,500.00 pesos gold, with a discount equivalent to the expenses of importing American money.

When the national money is redeemed in accordance with paragraph (b) indicated above, said money shall be physically withdrawn from circulation, remaining in the vaults of the bank charged with the management of the fund until it is released in accordance with the arrangement prescribed in paragraphs (c) and (d) of this same article, or until it is definitely withdrawn from circulation.

The premiums and discounts to which reference has just been made shall be fixed by the Monetary Commission created by this law.

Article 16. Profits earned through the operations of the fund of the

"Gold Standard Reserve" shall be accumulated in the same, and a statement of its condition shall be published monthly in *La Gaceta*.

Article 17. The Executive Power is authorized to make all arrangements necessary and convenient for the execution of this law, with the object of maintaining the stability of the established monetary system.

Article 18. The present law shall take effect upon its promulgation and repeals all previous laws or parts of laws inconsistent with the present.

Appendix G

VALUE OF THE SILVER IN THE PESO 25 GRAMS .900 FINE AT DIFFERENT PRICES FOR SILVER

(IN TERMS OF DOLLARS)

PRICE PER OUNCE TROY	GOLD VALUE OF SILVER IN PESO	PRICE PER OUNCE TROY	GOLD VALUE OF SILVER IN PESO
$ .50	$ .3617		
.51	.3689	.86	.6221
.52	.3760	.87	.6293
.53	.3834	.88	.6366
.54	.3906	.89	.6438
.55	.3978	.90	.6510
.56	.4051	.91	.6583
.57	.4123	.92	.6653
.58	.4195	.93	.6727
.59	.4268	.94	.6799
.60	.4340	.95	.6871
.61	.4413	.96	.6944
.62	.4485	.97	.7017
.63	.4557	.98	.7090
.64	.4630	.99	.7161
.65	.4702	1.00	.7233
.66	.4774	1.01	.7306
.67	.4847	1.02	.7378
.68	.4919	1.03	.7450
.69	.4991	1.04	.7523
.70	.5064	1.05	.7595
.71	.5136	1.06	.7667
.72	.5208	1.07	.7738
.73	.5281	1.08	.7812
.74	.5353	1.09	.7884
.75	.5425	1.10	.7957
.76	5498	1.11	.8029
.77	.5570	1.12	.8101
.78	.5642	1.13	.8174
.79	.5714	1.14	.8246
.80	.5786	1.15	.8318

Appendix G—*Continued*

PRICE PER OUNCE TROY	GOLD VALUE OF SILVER IN PESO	PRICE PER OUNCE TROY	GOLD VALUE OF SILVER IN PESO
.81	.5859	1.16	.8391
.82	.5931	1.17	.8463
.83	.6004	1.18	.8535
.84	.6076	1.19	.8608
.85	.6149	1.20	.8680
1.21	.8752	1.31	.9476
1.22	.8825	1.32	.9548
1.23	.8897	1.33	.9620
1.24	.8969	1.34	.9692
1.25	.9042	1.35	.9764
1.26	.9114		
1.27	.9186		
1.28	.9259		
1.29	.9331		
1.30	.9403		

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